LUDWIG VON MISSES
AND THE COMING OF
SOCIALISM IN AUSTRIA

by Bettina Bien Greaves

(The following was reconstructed from a variety of published and unpublished sources, including personal interviews with Ludwig von Mises, conducted by Mrs. Greaves over several years. The sources of the direct quotations are Mises’s own recollections, as recorded by the author.)

In the Vienna of Ludwig von Mises’s youth, political and economic trends were toward more and more government interference with the market, if not toward outright socialism. As a boy, young Mises heard about the conflict between the government and the radical Marxian socialists, or communists. When he was only eleven or twelve, so young that he had to look up the word “prostitution” in the dictionary, he read Women and Socialism, a popular, much-talked-about book by the Marxist August Bebel. Young Mises was an omnivorous reader and in time became “consciously anti-Marxian.”

However, when he entered the University of Vienna, he was an advocate of social reform like everyone else; if a government reform fell short of its goal, it was because not enough money had been spent or because the government had not been firm enough in enforcing the measure’s provisions.

One of Mises’s assignments at the University was to research housing conditions in Austria. The young student discovered that taxes on construction materials added to the cost of housing, rent controls made investment in housing unprofitable, and high taxes on capital gains kept venture capital from entering the housing market. Not only were fewer housing units available as a result, but fewer job opportunities were to be found in construction. Mises began to realize that the shortage and high cost of housing and construction materials were not the fault of business but of government interference. Capitalists, entrepreneurs, and builders wanted to open factories; they wanted to hire workers; they wanted to build houses; but they were hampered at every turn by taxes and government regulations. Mises’s study of housing led him to question all government intervention.

When Mises was a graduate student, the Marxists were agitating throughout Europe for a proletarian (worker) revolution. In Russia, the communists were trying to unite the workers to their cause. With the slogan “All the Land to the Peasants,” they appealed also to the peasants. They used terror as a weapon, calling strikes, robbing banks, and assassinating government officials. In Austria-Hungary, the socialists, members...
of the Social Democratic party, were permitted to demonstrate because the government had given them the "right to the streets." On November 28, 1905, about 250,000 "socialist workers" took to the streets. Led by Party officials, they marched past Parliament around the Ringstrasse in military fashion eight abreast. The city of Vienna was completely paralyzed.

That evening in a coffee house young Mises chanced to meet a fellow student named Otto Bauer. Mises was a critic of government intervention; Bauer was a devoted Marxist. Bauer was elated at the events. As a result of the workers' street demonstration, Bauer said, the Party had achieved "street autonomy." And they would defend this achievement, he said, "forever."

"What will happen," Mises asked, "if some day another party—using organized force—gains street autonomy? Wouldn't that mean civil war?"

"Only a bourgeoisie could ask such a question," Bauer responded. "A bourgeoisie who doesn't realize that the future belongs to us Socialists. What party would dare to confront the organized proletariat? Once we come to power, there will be no more resistance."

Several years later, as graduate students, Mises, the critic of government intervention, and Bauer, the dedicated socialist, both attended the University seminar of former Austrian Finance Minister Eugen von Böhm-Bawerk. Earlier Böhm-Bawerk had written a devastating critique of Marx's value theory, which had "morally wounded Marxian economics."

During the first semester of his economic seminar, Böhm discussed value theory. As seminar leader, Böhm played the role of chairman. While participating occasionally in the discussion himself, he encouraged seminar participants to speak up. Otto Bauer, the Marxist, did his best in the seminar sessions to refute Böhm's scholarly thesis. Böhm was serious and thorough. Bauer was brilliant, quick, and well informed. Back and forth the two men debated, while the other participants sat and listened. In the end, Bauer probably had to admit to himself that the Marxian labor theory of value did not hold up. Yet his Marxist faith and his determination to bring about a proletarian revolution remained unshaken.

After World War I, the old Austro-Hungarian armies were swept away by the chaos of defeat and revolution. Retreating troops broke discipline in their frantic efforts to return to their homes. Prisoners of war, their camps unguarded, were joined by politicians and common criminals. All scattered around the countryside seeking their homes through the shattered empire. Trucks and trains were commandeered by troops. Soldiers clung to the roofs and trains; many, literally hundreds, were swept off and killed as the trains passed through tunnels.

The ethnic conflicts that had torn the Austro-Hungarian Empire apart continued. Czechs trying to scramble aboard trains were tossed off as "traitors" by Hungarians. And vice versa. Every cultural, religious, linguistic group wanted to form an independent nation.

Before the War, Vienna had been the capital of the huge Austro-Hungarian empire. After the War, she was a large city in a small country with
no industrial base, a city occupied primarily by
government offices and unemployed bureaucrats.
The Viennese were impoverished, discouraged, de-
moralized. Inflation was wrecking their money
and destroying their savings. Many were unem-
ployed, starving, hungry. There were bread lines
and food riots. Once as a mounted policeman
was making his rounds in Vienna, his horse stumbed
and fell. A crowd immediately pounced on
the horse, killed it, and hacked it to pieces. The lucky
scavengers took chunks of horse meat home to
their hungry families.

The Allies' rigid blockade of the already starv-
ing Austrian population continued throughout the
hard winter of 1918. The blockade was even rein-
forced by Austria's old comrades in arms. The
Czechs and Poles cut off its coal and oil supplies.
The Hungarian, Czech, and Yugoslav governments
cut off its corn supplies. Defeat, revolution, disinte-
gration, blockage, starvation, denial of raw materi-
als and markets—such was the bitter pill Austria
was forced to swallow.

In the midst of this widespread destitution,
the Austrian communists offered a ray of hope.
The Communist Revolution had just taken place
in Russia. Communism was hailed as ushering in
a new utopia. Under communism, all property
would be commonly owned; there would be no
more poverty, hunger, or unemployment; there
would be neither "rich" nor "poor"; all would share
and share alike in the fruits of production. Com-
munist agitators in Vienna called on the people
to rebel, to take to the streets, to do away with pri-
ivate property, and join the march toward commu-
nism. Communism, or socialism, was "the wave of
the future."

Everyone was convinced that Bolshevism was
coming. They bent all their efforts on trying to ob-
tain good positions in the new order. The Catholic
Church and even the Social Democrats' opposition,
the Christian-Social Party, were ready to welcome
Bolshevism. So were businessmen. One prominent
Austrian industrial consultant announced that he
would rather serve the people than stockholders.
Bank directors and big industrialists looked forward
to being "managers" in a Bolshevist regime.

The pressure for socialism in Austria was hast-
tened along by developments in Hungary. There
the Bolshevists, with Bela Kun at their head, pro-
claimed on March 21, 1919, a "Dictatorship of the
Proletariat." They hailed the communization of
land, factories, shops, houses, bank accounts, and
even jewelry over a certain value. A leading official
of the Hungarian Soviet Republic proclaimed that
"by socializing private property throughout Hun-
gary, the Hungarian government has become the
richest and thus the most credit-worthy in the
world."

Mises's Marxist friend Otto Bauer was deter-
mined to bring about a proletarian revolution in
Austria similar to the one in Russia. Mises, by
then a severe critic of big government, was just as
determined to prevent a Bolshevik takeover of
Austria.

"You know what is at stake," Mises told Bauer.
"Austria cannot feed herself; she depends on im-
ports of food. If private property is confiscated
and private enterprises are socialized, production will
stop. Farmers will no longer bring produce to mar-
kets. Trade with foreign countries will come to a
halt. Within a few days Bolshevism in Vienna
would create starvation and terror. Plundering
hordes would soon roam the streets and a second
blood bath would destroy the remnants of Vien-
nese culture and civilization."

Mises met evening after evening with Bauer
and his wife, Helene Gumplowicz, to discuss these
problems. They agreed that Austria was in chaos,
that she was torn apart by conflicts of nationality
among persons of differing religions, cultures, and
languages. They knew it was imperative for Aus-
tria to improve production and trade. And they
agreed that workers sometimes had to migrate
to find work. However, they disagreed over
how to accomplish this without friction. Bauer
argued vigorously for a proletarian revolution,
and Gumplowicz encouraged and supported
Bauer in his determination. Communism,
they claimed, would alleviate economic suffering
and at the same time help to reduce national con-
licts. Mises sympathized with the plight of the
people but disagreed that a communist revolution
was the answer. Communism, Mises held, would
not, and could not, live up to the Bauers' expecta-
tions.

"The problem," Bauer argued, "is that under
capitalism the resettlement of workers follows the
blindly ruling laws of capitalist competition.
These laws violate the nationality principle and
the will of the nation. Under socialism, migration
would be consciously planned. With emigration
and immigration regulated deliberately, society
would gain power over its language and national
boundaries. Social migrations would then reflect
the will of the nation and no longer violate the na-
tionality principle and cause conflicts."
“But,” Mises responded, “if the deliberate regulation of the migration of workers is guided rationally, that is if economic efficiency is the goal, then it will sometimes have to go against the wishes of the people. If so, it too will lead to nationality problems.”

Bauer was not convinced. “Under socialism,” he said, “the deliberate regulation of migrations by the socialist community would take the place of those migrations that are dominated by the blindly prevailing laws of capitalist competition. Immigrants would be moved to places where they will increase the productivity of labor; workers will be induced to leave places where productivity is declining.”

“But that is precisely what competition accomplishes under capitalism,” Mises said. “If the planners in a socialist world state decide, for instance, that spinning and iron production were to be cut back in Germany and expanded in the United States, then German workers would have to be resettled in Anglo-Saxon territory. That could lead to national friction. To assume that the migration of workers across national boundaries, even when decided upon consciously and deliberately according to plan, would not lead to conflict under socialism, as it does under capitalism, is downright utopian.”

Mises continued. “Only if the socialist community is non-democratic, may we assume that no national frictions would arise. The people in such an undemocratic socialist society would be either planners or those who must submit to the plans. Such an undemocratic socialist society would be an empire of general servitude. It would keep the peace only by transforming the people into slaves.”

Mises reminded Bauer: “Bela Kun’s Bolshevist regime, launched in Hungary with such high hopes, has suffered economic and financial chaos, widespread starvation, and terror. It collapsed after little more than four months. Austria’s situation may be even more precarious than Hungary’s. At no time during the first nine months after the Armistice has Vienna had a supply of food for more than eight or nine days. Austria depends on the importation of food from abroad, which is possible only with the assistance of her former enemies. Without lifting a finger, they could force the surrender of a Bolshevist regime in Vienna.”

As a young man Otto Bauer had made up his mind never to betray his Marxian conviction, never to compromise. However, he was too intelligent not to realize that Mises was right. Thus, Mises was finally able to convince Bauer and Gumpowicz that a Bolshevist experiment in Austria would collapse in short order, perhaps in only a few days, and that Austria would be destroyed in the process.

The events lay in the hands of Otto Bauer, loyal Austrian and leader of the Social-Democratic Party. When Bauer presented his proposal to the Constituent Assembly in 1919, he called for “gradual” socialization only. Various schemes were drawn up for putting his program into execution, but none was ever adopted. Except for rent controls, which Bauer recognized expropriated the property of landlords, little actual socialization was put into effect in Austria. Mises had won his battle against the Bolshevist threat.

Publicly, Bauer attributed his rejection of socialization to Austria’s desperate economic plight and her dependence on foreign credit. Socialization, he admitted, had to be postponed because private trade was so much more superior at getting supplies into the country. Forced to choose between private capitalism and socialism, the socialist leader decided that, in an economically wrecked country, capitalism had to be repaired and maintained—at least for the time being. The alternative would have literally condemned thousands to starvation. In the end, it was Bauer’s rejection of the extreme communism he had advocated up until the end of World War I that saved Austria.

Because it was Mises who had persuaded Bauer to give up proletarian revolution as a goal, because it was Mises who had persuaded Bauer to compromise his extreme socialist principles, Bauer could never forgive Mises. The two men did not speak to each other ever again.
Conference Reports


The 1992 Allied Social Sciences Association meeting in New Orleans featured “The Road Back from Serfdom,” a special tribute to F. A. Hayek, with papers by Abram Bergson (Harvard University) on “Communist Economic Efficiency Revisited”; Ronald I. McKinnon (Stanford University) on “Spontaneous Order and the Road Back from Serfdom: An Asian Perspective”; and Sir Karl Popper (London School of Economics) on “The Communist Road to Self-Enslavement.” Janos Kornai (Harvard University) and George Mellan (The Wall Street Journal) were discussants. All the papers except Popper’s were published in the Spring 1993 issue of the American Economic Review; Popper’s appeared in the May/June 1992 issue of the Cato Policy Report. This year’s ASSA meeting in Boston included a session on “The Voluntary Provision of Public Goods,” organized by Randall Kroszner (University of Chicago), with papers by David Beito (University of Nevada, Las Vegas) and Daniel Klein and Chi Yin (University of California, Irvine) and comments by Donald McCloskey (University of Iowa) and Peter Boettke (New York University).

The Mises Institute’s annual summer instructional conference, the “Mises University,” was held in 1993 at Claremont McKenna College in Claremont, California. For the week-long conference, students chose individualized schedules from a list of thirty-eight lectures and ten seminars. The faculty were Roy E. Cordato (Campbell University), Thomas J. DiLorenzo (Loyola College, Baltimore), Roger Garrison (Auburn University), David Gordon, Jeffrey Herbener (Washington and Jefferson College), Hans-Hermann Hoppe, Yuri N. Maltsev (Cathay College), Murray N. Rothbard, Joseph T. Salerno, and Mark Thornton (Auburn University).

For information on the 1994 conference write the Mises Institute, Auburn, Alabama 36849.

Book Reviews

The Market, Competition and Democracy: A Critique of Neo-Austrian Economics

Stavros Ioannides
Edward Elgar, 1991

Reviewed by David Gordon

When a Marxist appraises Austrian economics, readers may expect unmitting hostility. Stavros Ioannides, a lecturer in Political Science at the Fandion University in Athens, undertakes this task and does not altogether disappoint. He regards the Austrians as ideologists of the New Right, and he constantly preaches the gospel according to St. Karl. But he is not altogether opposed to the Austrian approach. He finds much value in Austrian criticisms of neoclassical economics, a school which his Marxist confrères likewise reject. Further, he acquired in the course of his study a “love-hate relationship” (p. xi) with the work of F. A. Hayek.

While his interest in Hayek makes him more sympathetic to Austrian economics than is customary among Marxists, it at the same time endangers his project. Given that Hayek’s work encompasses many subjects besides economics, ranging from the nature of perception to the philosophy of law, Ioannides must decide whether he intends to write about Austrian economics or about Hayek’s system of thought. If he does both, he must be careful to distinguish the two subjects. Faced with this key decision, Ioannides blunders badly. He confuses Hayek’s philosophical views with the tenets of Austrian economics, moving from one to the other without discrimination.

This flaw emerges quickly in chapter two, “Origins and Methodological Principles of Neo-Austrian Theory.” He offers a detailed account of Hayek’s theory of social evolution, a matter outside the scope of economics proper. To his credit, Ioannides knows that not all Austrian economists
share Hayek's beliefs about unconscious rules and tradition, and he rightly stresses Mises’s rationalism as a contrast (p. 25). But he misses the fundamental point: Even if all Austrian economists in fact held identical opinions about the nature of law, the importance of tradition, and so on, these subjects would remain independent of economics. By the close of chapter two, then, I regarded Ioannides’s book with the utmost suspicion. This passage did not allay my misgivings: “It is easily seen, therefore, that the main methodological cleavage between Wieser and Böhm-Bawerk, on the one hand, and Menger himself, on the other, is the abandonment by the former of Menger’s individualist methodology” (p. 28). Has Ioannides read a line of Böhm-Bawerk’s explanation of value and price?

The next chapter, “Competition and Knowledge,” begins a pattern that continues throughout the remainder of the book. In every case, Ioannides contrasts the Austrian position with the neoclassical, awarding honors to the former. Alas, the Austrians, blinded by ideology, have failed to pursue their insights to the limit, and must in turn yield to the Marxists. Thus, for example, the Austrians rightly reject the model of perfect competition; competition is a process, not a state of equilibrium, and Hayek correctly maintains that “perfect competition is an abstraction which misses the most important aspect of competition, its dynamic nature” (p. 32). Furthermore, Kirzner’s stress on the entrepreneur exposes a vulnerable point in the neoclassical view, in that knowledge cannot be taken as fixed but constantly changes as entrepreneurs respond to and anticipate the uncertain future. Nevertheless, the Austrian view of competition ignores the fact that “the market process, by itself, constantly tends to objectify a great part of the knowledge which circulates in the economy” (p. 42). I take it that Ioannides means that once discovered, information becomes available for sale. This, in his view, topples the Austrian theory. Since people do not have the same access to new information, size becomes an advantage. Large firms acquire “objectified” knowledge and block their smaller competitors from access to it. Unable to compete, the smaller firms exit the market; and businesses in a capitalist economy increasingly grow larger.

Ioannides’s argument fails at each step. He does not distinguish between the perception of new opportunities and the results of that perception. Only the latter can become “objectified”; the former is precisely what is not available through a formula that can be “bottled and sold.” Ioannides can, if he likes, deny the existence or importance of entrepreneurial innovation; but to mount an effective argument he would at least need to understand the concepts at issue. More important, he offers no argument to explain why larger firms should be able to purchase this “objectified” knowledge at lower cost than their smaller rivals. Ioannides assumes exactly what he claims to prove, namely that larger firms are more efficient.

However mistaken Ioannides’s argument here, at least he attempts to support his views with reasons. Often his remarks do not rise to the level of mistakes. Thus the Austrian theory of capital must be rejected, he claims, because it is not “dynamic.” A dynamic theory is one able to “sustain the notion of a cyclically repeated process of production” (p. 101). This is merely a stipulative definition of “dynamic”; why would capital ever reproduce itself automatically? Elsewhere, he chides the Austrian theory of money for failing to separate money fully from other media of exchange; the Austrians view money as a commodity and not unique. But why must an acceptable theory uphold “the uniqueness of money” (p. 115)? Presumably, because Marx told us so. Elsewhere, Ioannides offers the following objection to the Austrian theory of the business cycle: “[t]rade cycles [in the Austrian theory] are not caused by the market process itself but are, instead, produced by exogenous manipulation of the money supply” (p. 133). To him, a correct theory of the cycle must view crises as inherent in a capitalist economy.

In the final three chapters Ioannides confuses Hayek’s social philosophy with Austrian economics. He first addresses the socialist calculation argument, and surprisingly for a Marxist, he does not hold that the argument fails on its own terms. Rather, he claims that both Mises and Hayek on the one hand, and Lange and Lerner on the other, ignore the real issue. The arrival of socialism does not depend on the success or failure of abstract models of the economy. Instead, historical reality must be consulted. If we examine history wearing proper Marxist spectacles, we shall see that state intervention is necessary to promote the reproduction
of capital. Further, “participation in the market process is inconceivable if the participant is not an owner of resources. Therefore, state interventionism and state ownership are bound to be complementary concepts” (p. 164). Thus, capitalism leads to socialism.

Even if this farrago were right, what about the calculation argument? The contention that socialism is inevitable does not refute the claim that socialism spells disaster. Ioannides does not, however, concern himself with such narrow technicalities as whether socialism can work. Instead, he is worried that the capitalist system is undemocratic. If people have property rights that are not subject to majority control, then the will of the people has been thwarted. The rule of law which Hayek favors “amounts to the absolute elimination of the sphere of politics” (p. 149), and as such is totalitarian. Hayek and the neo-Austrians surrender all power to the capitalists, “with society as a whole not even having the right to express an opinion” (p. 155).

We see here a graphic result of failure to delimit the topic at hand. Whatever the value of Hayek’s political philosophy, Ioannides’s attack on it ignores the issue of economic theory raised by the Austrians. Whether or not the will of the majority should be restricted, the question remains: Can socialism solve the calculation problem? If it cannot, how will its conformity to the political imperatives Ioannides supports enable it to avoid economic disaster? Ioannides might have confronted this issue had he grasped the elementary points that Hayek’s political philosophy is not part of Austrian economics, and that adherence to Austrian economics does not commit one to any particular political views. Mises, for example, favored just the sort of majority-rule democracy Ioannides endorses; but it does not follow from this fact that Mises’s version of Austrian economics, as against Hayek’s, is “democratic.” Normative political judgments must be kept apart from economic analysis.

Considered as political theory, Ioannides’s remarks are pretty poor stuff. If the majority of a society wishes to exterminate an ethnic minority, is it totalitarian for constitutional restraints to prevent it from carrying out its democratic will? If people have property rights, why should these rights be subject to what Ioannides is pleased to call “social” control? Further, it does not follow from the fact that a political system restricts the power of the majority that anyone’s freedom of opinion is restricted. What prevents people in a Hayekian society from publicly advocating its replacement by socialism?

As if all of this were not enough, the book’s style can hardly be termed “user-friendly.” The reader frequently faces sentences like “It is obvious that every member of society enjoys the right to express an opinion on the social system only once in his/her lifetime when, at the age of 45, he/she is called upon to elect some of his/her peers to the legislative assembly” (p. 149). Ioannides has read extensively in the Austrian literature, and his obvious effort to be fair to his political opponents deserves respect. But he lacks the resources to carry out successfully the difficult task he has set for himself. As a result, he displays incompetence in an unusually wide variety of fields.

The Guardian of Every Other Right: The Constitutional History of Property Rights

James W. Ely, Jr.
Oxford University Press, 1992

Reviewed by John V. Denson

Ludwig von Mises called the private ownership of property and its protection the cornerstone of a free society, and the historian Edward Gibbon observed that “[t]he enslavement of man usually begins in the economic sphere.” The truth of these ideas concerning property and liberty are demonstrated in an excellent new book, The Guardian of Every Other Right: A Constitutional History of Property Rights, by James W. Ely, Jr. The author associates the decline and fall of American property rights with the New Deal. This compact, well-researched and well-documented history is published in paperback by Oxford University Press as a part of the Organization of American Historians Essays on the Bill of Rights series.

James W. Ely, Jr. is professor of law and history at Vanderbilt University. His prose is concise and clear to the general reader, but the legal scholar will find a treasure trove of research in the footnotes and an excellent bibliography. The book’s title is quoted from one Arthur Lee of Virginia, who declared during the Revolutionary Era that “[t]he right of property is the guardian of every other right, and to deprive a people of this right, is in fact to deprive them of their liberty” (p. 26).

The primary theme of the book is that property and economic rights are inseparable parts of
individual liberty, a concept taken from Locke and incorporated into the original meaning of the U.S. Constitution. As Ely notes:

The book performs a biopsy on property rights and finds a cancerous growth in the form of the New Deal. This biopsy (hopefully not autopsy) reveals that the New Deal attacked property by separating it from other individual or human rights (freedom of speech, the right of assembly, and so on) and after making this division, conquered it by reducing property rights to a lesser status unprotected by the Constitution. The infamous shift by the U.S. Supreme Court, beginning with the Carolene Products case in 1937, was labeled by one writer as "the switch in time which saved nine." Ely cites the great constitutional lawyer, John W. Davis (the 1924 Democratic nominee for President) as a courageous opponent of this shift by the New Deal Supreme Court. Davis took issue with the separation of property rights from other human rights: "The two are not antagonistic, but parts of one and the same thing going to make up the bundle of rights which constitute American liberty. History furnishes no instance where the right of man to acquire and hold property had been taken away without the complete destruction of liberty in all of its forms."1

Ely provides an excellent overview of Supreme Court decisions from about 1890 through 1936, a period when the Court, mainly under the leadership of Justice Stephen Field, constitutionalized the laissez-faire approach to property rights. New Deal critics of the laissez-faire Supreme Court charged that the Court had created these property rights out of thin air. The New Deal advocates criticized the Court for failing to see the change in economic and ethical values as America became wealthy and a great industrial power in the early part of the twentieth century. These critics alleged that they were taking a higher moral and ethical ground by providing for a redistribution of wealth on a more equitable basis. Ely refutes this position by showing the basis upon which the Supreme Court had protected property rights from the time of the adoption of the Constitution.

The book takes the reader through the Jeffersonian and Jacksonian periods with the explanation that Jeffersonian "equality" meant "equal rights for all, special privileges for none." The Jacksonian period continued this tradition of equality in individual rights, attacking those who would use government to benefit the privileged few. Jackson further observed that "[e]quality of talents, of education, of wealth cannot be produced by human institutions," and thus opposed the egalitarians of his time. Reformers who subscribed to the laissez-

[...] of all the special legislation sought and acquired by business interests, the protective tariff was the most colossal fraud. Repudiating the fiction that the tariff was designed to protect the wages of American workers, its laissez-faire opponents characterized it as "the aggrandizement of capital by law," and abuse of the taxing power by special legislation. Laissez-faire reformers warned capitalists that protectionism was the parent of socialism. "It is a significant fact that the agitation of the labor question in this country comes most urgently from persons employed in those branches of occupation which are most affected by a protective tariff."2

Benedict also mentions the famous dissenting opinion of Oliver Wendell Holmes in the Lochner case (1905). Holmes stated that the U.S. Constitution did not adopt any particular economic system, nor did it adopt Herbert Spencer's Social Statics. Benedict observes that while the Constitution may not have adopted a particular economic system as in Adam Smith's Wealth of Nations, the Constitution did consider property to be a basic individual right, as did Spencer. Spencer's book, Social Statics, talked about the "law of equal freedom," and property was merely one of the basic human rights. While the Constitution did not adopt a specific economic system, it did require that any economic system implemented respect property rights.
Ely's book could be improved with more emphasis on the disastrous effects of war on property rights, and particularly to the destruction of economic rights which occurred as a result of World War I. He does document that in 1861 the U.S. government had its first income tax, a flat rate of 3% on income over $800, and that "[t]he exigencies of the Civil War necessitated widespread impairment of existing economic arrangements." (p. 82.) He further documents how the Civil War upset the balance of power between the federal government and the states when the South lost all of its political restraint upon the flow of power to the central government. Furthermore, he notes that "In no un- and Welfare Century." It was one of the Framers, James Madison, who correctly identified the problem of war related to liberty and economic rights:

"..."Of all the enemies to the public liberty, war is, perhaps, the most to be dreaded, because it comprises and develops the germ of every other. War is the parent of armies; from these proceed debts and taxes; and armies, and debts, and taxes are the known instrument for bringing the many under the domination of the few." 3

According to the preface, the book is designed for use by undergraduates; hopefully it will be widely used in our colleges. In its provision of extensive references to both proponents and opponents of property rights, the book outlines research necessary for proponents of individual liberty to re-establish Constitutionally protected property rights in America. The book merits close study, and hopefully will gain the widespread recognition it deserves. One reviewer, the University of Maryland historian Herman Belz, has already stated that Ely's book "is further evidence of the conservative challenge to liberal orthodoxy that has emerged in recent years in American historiography. That the book appears under the co-sponsorship of the Organization of American Historians, one of the more militantly liberal scholarly associations in the United States, is a small but significant sign of the change in intellectual climate." 4


Socialism Revised and Modernized: The Case for Pragmatic Market Socialism
James A. Yunker
Praeger, 1992

Reviewed by Charles N. Steele

While schemes for central planning are making something of a comeback in economic theory, James A. Yunker's book Socialism Revised and Modernized attempts something a bit different. Professor Yunker presents us with a detailed proposal for a national experiment with "pragmatic market socialism." This new socialism is not quite what we might expect, however. In Yunker's words:

"It must be tirelessly reiterated that pragmatic market socialism does not involve Soviet-style central planning, or any other type of national or even indicative planning; that it does not imply a giant, paternalistic welfare state; that it does not intend radical redistribution and egalitarianism; that it has no communistic aspirations; that it would not signify the triumph of bureaucratic homogenization over a healthy level of individualistic materialism." (p. 281)

What, then, is pragmatic market socialism? Yunker's starting point is that capitalism is plagued by a serious ethical liability: All income derived from ownership of capital is unearned and hence immoral. It is particularly outrageous, in his view, that anyone should be able to live off capital property income. Only labor income is truly earned and therefore just. Furthermore, Yunker believes that private ownership of capital is unnecessary for the economy to function as it does. Thus he calls for public ownership of all capital goods (with certain exceptions, discussed below).

Yunker does recognize that capitalism has been tremendously successful in raising living standards for everyone. He argues that "the level of economic efficiency and social welfare in the advanced capitalist nations is... extraordinarily
high, relative to any time or place in human history” (p. 13). His problem, then, is to develop a system of public (government) ownership of capital which will not disturb the functioning of the existing economic order—there must be no central planning of any form, no radical equalization of wealth or labor income, no reorganization of business for goals other than profit maximization, and so on. Yuncker states clearly that he wants his system essentially to duplicate modern capitalism, with the exception of private ownership of capital.

Yuncker’s solution, in brief, is that all capital ownership be turned over to the government, with the exceptions of small businesses (broadly defined), the press (so as to avoid government control of information and news), and something called “entrepreneurial businesses,” which are those founded by an individual and which remain private so long as the founder is actively managing them. Excepting these, all corporations and firms are to be owned by the Bureau of Public Ownership (BPO), a government agency.

The BPO is the heart of Yuncker’s system. It is to be a two-tiered organization, divided into a central office and numerous decentralized local offices. The central office has two primary functions: it compiles national business statistics, and it receives dividend payments from firms and pays them back out to wage earners as a “social dividend” proportional to their labor incomes. A small amount of this money—Yuncker estimates five percent—is kept by the BPO to cover its administrative costs. This office also levies a “capital use tax” on all firms not owned by the BPO.

The second level of the BPO is the real key to Yuncker’s plan. He envisions several hundred local BPO offices, each staffed with ten or so BPO agents, each agent responsible for ten or so corporations. The task of an agent is to monitor the economic performance of the corporations under his jurisdiction. If a corporation fails to perform well, (that is, to make profits), the agent can fire the CEO or more of top management. Corporate management would continue to function as under capitalism, including the decision whether or not to pay dividends (to the BPO). The BPO agents would receive a percentage of corporate capital income, ensuring their interest in high profits. Also, BPO personnel at all levels would be forbidden by law from attempting to dictate how a corporation is to be run, so as to prevent the system from becoming centrally planned.

There is a great deal more to the proposal—

“pragmatic market socialism” is Yuncker’s life’s work, and has been thirty years in the making—but this captures the essence of the system. What can be said of it? I will restrict my comments to the sphere of economics, while noting that Yuncker’s position on the ethics of private capital ownership, as well as the role of government, could certainly be challenged.

The two main criticisms which have been leveled at socialism from the standpoint of economics are the Austrian calculation argument and the public choice view that socialism is plagued by endemic rent seeking. Yuncker is quite conscious of the charge that central planning does not work because planners cannot calculate, and he has gone to great lengths to avoid central planning of production. In his view, capital markets would continue to exist under pragmatic market socialism, with publicly owned corporations trading among themselves. Competition for profits and the threat of bankruptcy would keep corporations from becoming inefficient, and the provision for private “entrepreneurial business” is designed to ensure that the system not become stagnant. One could debate whether Yuncker’s system, as designed, would constitute a functioning market system, but such a debate would likely revolve around marginal details. In my view, the essential point is that Yuncker seeks to avoid establishing any centralized control of the economy, and presumably he would willingly change his system were it shown to contain inherent elements of planning.

What of the charge that socialist systems are by nature subject to endemic rent seeking? Yuncker
proposes placing all capital and all production under a single government bureau. Control of that bureaucracy would potentially be extraordinarily valuable, much more so than the capture of any bureaucracy in, say, present-day America. Were this system to be implemented, one would expect vast amounts of resources to be spent by those competing for control of the BPO. Even worse, anyone controlling the BPO would have great incentive to modify Yunker’s finely tuned system for personal advantage. This would be simple, even without bureaucratic capture—Congress need only slightly amend Yunker’s “Act for Economic Justice” and the system could quickly become a de facto central planning system, or even one de jure. And certainly it is not going too far to say that there are many groups today, including Congress, that might be willing to usurp a system such as Yunker’s for short-run personal gain.

Yunker’s response to this sort of criticism is to dismiss it as “dogmatic” and “begging the question” (p. 79), and “exceptionally closed-minded” (p. 85). But the questions are neither dogmatic nor trivial. Yunker proposes to establish a government bureau, capture of which would potentially give one control of the entire economy, and a system of rules which, were it not followed to the letter, or where changed slightly, would yield some sort of centrally planned system. He “solves” this problem by declaring that this would all be forbidden by statute. He thus ignores an important body of well-defined economic theory—public choice—which should have figured prominently in his endeavor. The result is that his carefully constructed system contains gaping holes.

A word must be said about Yunker’s view of Austrian economics. He devotes a fair amount of attention throughout the book to Austrians, including one nineteen-page section (pp. 175–93). This might have been interesting, but unfortunately he displays little understanding of the Austrian tradition, and his discussions consist primarily of fatuous invective. For example, he speaks of the “Austrian school of institutional economics” (p. 23) and in characterizing Austrianism gives a brief and accurate definition of (old) institutional economics. Institutionalism, of course, is an American variant of Hirschianism, the traditional antithesis of Austrian economics. It is ironic, amusing, and absurd that Yunker should confuse the two.

With similar depth of understanding, Yunker condemns the work of Mises and Hayek in the socialist calculation debate as “gaseous, opinionated, confused, and inconclusive speculation” (p. 177).

Oddly, he also seems to think they were correct, and that socialism must absolutely avoid central planning. He misunderstands Kirzner’s theory of entrepreneurship, incorrectly assuming it to be a theory about a career role for people with money (p. 102), rather than a theory about a kind of human action engaged in by all participants in an economy, irrespective of resource ownership. The rest of his discussion of the Austrian school is in the same vein: It is so misinformed as to be entirely irrelevant. He was too busy redesigning the world to acquaint himself with the subject.

What, then, can be said about Yunker’s book? In many respects it is an impressive work. He obviously has given great thought and effort to constructing his scheme, and he has pursued his goal singlemindedly, even fanatically, and avoided being sidetracked into plans to reconstruct all of society. He desires only to abolish his personal bugaboo, the private ownership of capital, and that is all that his system is designed to do.

Recommended Reading

(In this feature of the AEN, a variety of scholars list the most interesting books, articles, or working papers relevant to Austrian economics they have recently encountered.)

Peter J. Boettke
Assistant Professor of Economics
New York University

The breakdown of communism in the late 1980s has left many Sovietologists struggling to explain the failure of the economics profession to understand the structural problems in the Soviet system (both in politics and economics), let alone the failure to predict the collapse. The Spring 1993 issue of The National Interest contains particularly insightful articles by Martin Malia, Robert Conquest, and Peter Rutland. Rutland, for example, states that “[c]riticisms of Sovietology for political bias, a tendency to ignore émigrés, and lack of scholarly rigor have some validity. However, even taken together they still do not get to the root of the problem, which I see as the emergence of a ‘disciplinary groupthink’ which stifles creative thinking and controversial ideas. From this perspective, Sovietology is not an aberrant
case, but is symptomatic of a general crisis besetting the social sciences." This message should resonate with Austrians who are trying to push an alternative perspective on economic problems.

On the issue of the transformation of the former socialist economies to market economies I highly recommend the journal Communist Economies and Economic Transformation, published by the Centre for Research on Communist Economies in London. Many insightful articles—reflecting a strong Austrian influence—have appeared in this journal over the past few years. See, for example, Vitalii Naishul, "Liberalism, Customary Rights and Economic Reforms," in volume 5, no. 1 (1993).

The issues of the transformation are also addressed from a variety of perspectives in Social Philosophy and Policy (vol. 10, no. 2, 1993). Economic and political liberalism are given a good hearing in this volume. Despite the collapse of communism, however, many refuse to let go of socialism. The title of Joseph Stiglitz's Wicksell Lectures, forthcoming from MIT Press, is Whither Socialism? Stiglitz, perhaps the premier mainstream economic theorist of the day, concludes these lectures by asking if modern economics can serve the ideals that motivated socialism (egalitarianism, for example). He answers in the affirmative. Stiglitz is not an aberration: Pranab Bardhan and John Roemer construct a new model of market socialism which they believe eliminates the undesirable aspects of both existing socialism, as practiced in the Eastern bloc, and existing capitalism, as practiced in the U.S. Their model introduces political and economic competition while retaining public ownership. See Bardhan and Roemer, "Market Socialism: A Case for Rejuvenation," Journal of Economic Perspectives 6 (Summer 1992). See also Roemer, "The Morality and Efficiency of Market Socialism," Ethics (April 1992). Misesians must address these modern arguments for socialism (based on contemporary information economics) head on. An attempt to deflect Misesian objections to market socialism can be found in James Yunker, Socialism Revised and Modernized (Praeger, 1992); [reviewed in this issue].


One of the most interesting developments in the book world is the Cambridge University Press series The Political Economy of Institutions, edited by Douglass North and James Alt. Notable contributions include North's Institutions, Institutional Change and Economic Performance (1990) and Jack Knight's Institutions and Social Conflict (1992). Austrians will find much of interest in this series, as well as much to disagree with. Along with the series Studies in Rationality and Social Change (Cambridge), edited by Jon Elster, the Alt and North series represents a significant development in the literature that seeks to resurrect grand theory in the social sciences.

Richard N. Langlois
Professor of Economics
University of Connecticut

Brian J. Lossby, Equilibrium and Evolution: An Exploration of Connecting Principles in Economics (Manchester University Press, 1991). This new work by the author of Choice, Complexity and Ignorance (Cambridge, 1976) is based on lectures given at the University of Manchester. It is full of Lossby's characteristic insight about firms, markets, economic theory, and the history of economics.

Thomas M. Jorde and David J. Teece, eds., Antitrust, Innovation, and Competitiveness (Oxford, 1992). This collection of essays by important figures in the economics of antitrust is
significant because, as crafted by its editors, it is largely critical of antitrust theory and policy for neglecting innovation and failing to see competition in dynamic terms.

Richard R. Nelson, ed., National Innovation Systems: A Comparative Analysis (Oxford, 1993). This is an important volume of commissioned essays surveying "national innovation systems"—the interplay of government, industry, and the economy—in fourteen countries of various sizes around the world. The most controversial chapter is probably that on Japan, by Japanese economists Hirohiko Odagiri and Akira Goto. The authors reject the dominant Western view that government support was at the heart of Japanese success, arguing instead for the importance of free competition. They also document the declining role of the Japanese government in recent years.

Donald N. McCloskey, ed., Second Thoughts: Myths and Morals of U. S. Economic History (Oxford, 1993). This book of short essays by eminent economic historians takes aim at almost all the venerable icons of American economic history. For some people, a better title might be: Everything You Thought You Knew About American Economic History was Wrong. The topics are too numerous even to survey, and the essays are uniformly interesting; but I especially recommend McCloskey’s own essay on the rhetoric of industrial decline, which, as usual, is a delightful bit of writing.

Finally, I mention Morris Silver’s book Enterprise and the Scope of the Firm (Martin Robertson, 1984). Although this book is almost ten years old, it is not as well known among Austrians. It should be, as it presents the first clear attempt to set out an Austrian theory of vertical integration, one heavily influenced by a Kirzner–Schumpeter view of entrepreneurship. This book helped galvanize my own thinking on the subject early on, and it has been an important influence on my work.

New and Noteworthy

(Other recent books and articles of interest, recommended by the staff of the AEN. Readers are encouraged to forward their suggestions to the editor.)

Bruce J. Caldwell and Stephan Boehm, eds., Austrian Economics: Tensions and New Directions (Kluwer, 1992). This new collection offers reflection, self-criticism, and proposed new directions for Austrian research. Focuses mainly on philosophical and methodological aspects of Austrian economics. Contributors include Stephan Boehm on the historiography of the Austrian school; Uuskali Mäki on the "realism" of Austrian theory; Martin Ricketts on entrepreneurship; Jeremy Shearmur on subjectivism; Brian Lossby on market coordination; Richard Langlois on organization and institutions; Alan Hamlin on welfare economics; and Ulrich Witt on Austrian economics and evolutionary theory. Israel Kirzner, Mario Rizzo, Lawrence White, Mark Blaug, Bruce Caldwell, and Robert Sugden are also featured.

Brian C. McCormick, Hayek and the Keynesian Avalanche (St. Martin’s Press, 1992). Comprehensive account of Hayek’s disputes with Keynes and the Cambridge school on money, capital, and business cycles, beginning with Hayek’s arrival in London in the early 1930s and continuing throughout the “neoclassical synthesis” of the post-war years and the crisis of Keynesian economics in the 1970s and 1980s. Hayek’s early relationship with Keynes is embedded in a larger debate between the London School of Economics and Cambridge traditions. The author digs up a lot of detail, like Hayek’s syllabi for several courses at L. S. E. in the 1930s.


Gary Lawson, “Efficiency and Individualism,” Duke Law Journal 42, no. 1 (October 1992): 55–87. Informed, thoughtful critique of “social efficiency” as used in law and economics. Adopts explicitly Misesian notions of methodological individualism and subjectivism and exposes the difficulties in Pareto optimality, “social wealth” maximization, and surprisingly, the modern Austrian idea of “plan coordination.” Concludes that “a conception of social efficiency that is simultaneously coherent, robust, and economic is simply not to be found.”

based on maximization of broader social objectives, regardless of their effects on individual welfare. "(E)very durable social institution or practice is efficient, or it would not persist over time." The U. S. sugar subsidy program, for example, which costs taxpayers around $3 billion a year, is "the tested way in which the domestic sugar-beet, cane, and high-fructose-corn producers can increase their incomes by perhaps a quarter of the $3 billion—the other three quarters being deadweight loss..." The [Chicago] theory would say that the sugar program is grotesquely inefficient because it fails to maximize national income. Maximum national income, however, is not the only goal of our nation, as judged by the policies adopted by our government—and government’s goals, as revealed by actual practice are more authoritative than those pronounced by professors of law or economics." The sugar program, then, is efficient: "It has stood the test of time."


Peter J. Boettke, Why Perestroika Failed: The Politics and Economics of Socialist Transformation (Routledge, 1993). Boettke's analysis of perestroika combines Austrian insights on the problem of economic calculation under central planning with a public choice analysis of the political maneuvering involved in the transformation of the Soviet system in the late 1980s. Gorbachev's reforms, he argues, were doomed to failure because they ignored problems of calculation, credible commitment and renegotiation, and the political marketplace.

Richard H. Timberlake, Monetary Policy in the United States: An Intellectual and Institutional History (University of Chicago Press and Cato Institute, 1993). History of U. S. monetary policy from the establishment of the Federal Reserve System in 1914 to the present. Successor to Timberlake's earlier work The Origins of Central Banking in the United States. Also includes discussions of the debate on legal tender laws that arose during and after the Civil War, how the present central banking system has its origins in the First and Second Banks of the United States; and how the Banking Act of 1935 and the Monetary Control Act of 1980 each increased the scope and power of the Fed.

Larry J. Sechrest, Free Banking: Theory, History, and a Laissez-Faire Model (Quorum Books, 1993). Defense of free banking, framed as a discussion of Say's Law. Claims that monetary equilibrium can only be achieved under a free-banking regime. Broadly follows the White-Selgin model but differs from those authors in the interpretation of both the Scottish and early American experiences with free banking. Argues that the most likely form of free banking that would emerge today would be a fractional-reserve system, with banks issuing notes convertible in specie.

Sheila C. Dow and John Smithin, "Free Banking in Scotland, 1695–1845," Scottish Journal of Political Economy 39, no. 4 (November 1992): 374–90. Surveys the debate between White, Dowd, Rothbard, and Sechrest on the viability of the Scottish banking system before Peel's Act and its use as a historical defense of free banking. Argues that the Scottish system was indeed "free" but not perfectly competitive and thus subject to widespread market failure, inevitably leading to excessive concentration.

Daniel S. Hamermesh, "The Young Economist's Guide to Professional Etiquette," Journal of Economic Perspectives 6, no. 1 (Winter 1992): 169–78, and idem, "Professional Etiquette for the Mature Economist," American Economic Review 83, no. 2 (May 1993): 34–38. Essential reading, of the What-They-Didn't-Teach-You-in-Graduate-School variety. The author, a mature economist, offers advice to younger colleagues just entering the profession, and to those who are already established, on the appropriate procedures for presenting and publishing research (i. e., how to solicit feedback, whom to acknowledge, how to select a journal, what to do about acceptances and rejections for publication); commenting on other people's work (how to make informal suggestions, how to write a referee report); writing letters of recommendation; constructing a résumé and searching for a new job; and other essential professional matters.
UPCOMING EVENTS

Association of Private Enterprise Education
“Liberty, Markets, and Economic Progress”
April 10–12
San Antonio, Texas

Ludwig von Mises Institute
“The Costs of War”
May 20–22
Atlanta, Georgia

Western Economic Association
“Markets and the Environment”
June 29–July 3
Vancouver, British Columbia

Ludwig von Mises Institute
“Mises University”
July 16–23
Claremont, California

Southern Economic Association
November 20–22
Orlando, Florida

Bruce J. Caldwell, professor of economics at the University of North Carolina, Greensboro, is editing two volumes of the Hayek Collected Works (University of Chicago Press and Routledge): vol. 9, *Contra Keynes and Cambridge*, and vol. 10, *Socialism and War*, each with the subtitle “Essays, Correspondence and Documents.” Caldwell is spending the Spring 1994 semester at Cambridge (U. K.) as a Clare Hall Visiting Fellow, where he will continue his work on Hayek while participating in the seminar run by Tony Lawson, a Post Keynesian interested in Hayek and “scientific realism.”

Parth Shah, assistant professor of economics at the University of Michigan, Dearborn, has been named chair of the economics group within the Department of Social Sciences. Parth presented his paper “The Role of Bankers in Economic Development” at New York University’s Austrian Economics Colloquium in October.

Mark Thornton, O. P. Alford III Assistant Professor of Economics at Auburn University, has been named Auburn University Coordinator for Academic Affairs at the Mises Institute. Thornton also heads the Institute’s Political Economy Club, which holds a Brown Bag Seminar on Wednesdays in the Institute library. When you’re in the Auburn area (1 1/2 hrs. from Atlanta), you’re welcome to attend (or propose to present a paper). Recent seminars have included Henry Thompson on NAFTA, Robert Hébert on economics and purgatory, Liam Ford on media and government, Lew Rockwell on the school voucher debate, Madison Jones on the politics of the Southern literary tradition, Jeffrey Tucker on Lord Acton’s opinions of America, and James Kee on problems of modern business education.


Notes and Transitions

We regret to report the death of David Osterfeld in October. Osterfeld was professor of political science at St. Joseph’s College in Rensselaer, Indiana, and a contributor to the *Austrian Economics Newsletter*, the *Review of Austrian Economics*, and numerous other scholarly publications. His most recent book was *Prosperity versus Planning* (Oxford University Press, 1992), a critique of development planning.

Roger W. Garrison, associate professor of economics at Auburn University, was interviewed as the Austrian school representative for A Modern Guide to Macroeconomics: An Introduction to Competing Schools of Thought, edited by Peter Wynarczyk, Brian Snowdon, and Howard Vane (Edward Elgar, 1994). Other figures interviewed for the collection include Robert Barro, James Tobin, N. Gregory Mankiw, Stanley Fischer, David Laidler, Milton Friedman, Robert Skidelsky, Edmund Phelps, Robert Lucas, and Charles Plosser. Garrison’s paper “Hayekian Trigonometry and Beyond” is forthcoming in the volume *Hayek, Coordination and Evolution*, edited by Jack Birner and Rudy van Zijp (Routledge, 1993), while his article on “Keynesian Splenetics” was published in the Fall 1992 issue of *Critical Review*. 

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