

Ludwig von Mises and the Austrian School of Economics

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Everyone carries a part of society on his shoulders: no one is relieved of his share of responsibility by others. And no one can find a safe way for himself if society is sweeping towards destruction. Therefore everyone, in his own interests, must thrust himself vigorously into the intellectual battle. No one can stand aside with unconcern: the interests of everyone hang on the result. Whether he chooses or not, every man is drawn into the great historical struggle, the decisive battle into which our epoch has plunged us (Mises 1988, p. 169).

This is the message of Ludwig von Mises. No one has ever fought the battle more courageously than Mises, nor had a more decisive long-run effect. Murray Rothbard is correct when he says “. . . if the world is ever to get out of its miasma of statism, or, indeed, if the economics profession is ever to return to a sound and correct development of economic analysis, both will have to abandon their contemporary bog and move to that high ground that Mises developed for us” (Rothbard 1983, p. 5).

Now, as the battle appears to be turning in favor of freedom, is an appropriate time to reconsider the role of economic theory in these world-wide changes. Specifically, it is time to consider the work of Mises and the Austrian school in the development and dissemination of the economic principles of social progress. Two steps are necessary to complete this task. The first is to demonstrate the pre-eminence of the Austrian school in developing the principles of free enterprise. The second is to demonstrate that Mises is the champion of this tradition in the twentieth century.

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Method and the Austrian Tradition

Carl Menger founded the Austrian school during the marginalist revolution of the late nineteenth century in his attempt to correct the errors of the classical economists. As Menger said:

Adam Smith and this school have neglected to reduce the complicated phenomena of human economy in general, and in particular of its social form, "national economy" to the efforts of individual economies, as would be in accordance with the real state of affairs. They have neglected to teach us to understand them theoretically as the result of individual efforts. Their endeavors have been aimed, rather, and to be sure, subconsciously for the most part, at making us understand them theoretically from the point of view of the "national economy" fiction. On the other hand, the historical school of German economists follows this erroneous conception consciously (Menger 1985, pp. 195-96).

It is the adherence to these methodological precepts of individualism and essentialism that distinguish the Austrian school from all others. Although Mises significantly refined and improved his position, Menger laid the groundwork:

This is the ground on which I stand. In what follows I have endeavored to reduce the complex phenomena of human economic activity to the simplest elements that can still be subjected to accurate observation, to apply to these elements the measure corresponding to their nature, and constantly adhering to this measure, to investigate the manner in which the more complex economic phenomena evolve from their elements according to definite principles (Menger 1976, p. 47).

It is now the task of the reader to judge to what results the method of investigation I have adopted has led, and whether I have been able to demonstrate successfully that the phenomena of economic life, like those of nature, are orderly strictly in accordance with definite laws (Menger 1976, p. 48).

Via this method, Menger solved the paradox of value, derived the subjective theory of value, developed a unified theory of price and reconstructed the origin of social institutions such as money, markets, property, and law. More than this, he began the process, culminating in the work of Mises, that has resulted in universally correct economic laws of social systems. As Menger stated:

The aim of this orientation, which in the future we will call the *exact* one, an aim which research pursues in the same way in all realms of the world of phenomena, is the determination of strict laws of phenomena, of regularities in the succession of phenomena which do not present themselves to us as absolute, but which in respect to the approaches to cognition by which we attain to them simply bear within themselves the guarantee of absoluteness (Menger 1985, p. 59).

In contrast, most other schools of economic thought deny, because of their methodological positions, the existence of universal laws of economics. Most prevalent are empirically based schools such as the German historical school that Menger fought. Menger was quite clear on this:

If, therefore, exact laws are at all attainable, it is clear that these cannot be obtained from the point of view of empirical realism, but only in this way, with theoretical research satisfying the presuppositions of the above rule of cognition.

But the way by which theoretical research arrived at the above goal, a way essentially different from Bacon's empirical-realistic induction, is the following: it seeks to ascertain the *simplest elements* of everything real, elements which must be thought of as strictly typical just because they are the simplest.

The specific goal of this orientation of theoretical research is the determination of regularities in the relationships of phenomena which are guaranteed to be absolute and as such to be complete.

It examines, rather, how more complicated phenomena develop from the simplest, in part even unempirical elements of the real world in their (likewise unempirical) isolation from all other influences . . .

Science starts out, however, with these assumptions, since it would never be able otherwise to reach the goal of exact research, the determination of strict laws. On the other hand, with the assumption of strictly typical elements, of their exact measure, and of their complete isolation from all other causative factors, it does to be sure, and indeed on the basis of the rules of cognition characterized by us above, arrive at laws of phenomena which are not only absolute, but according to our laws of thinking simply cannot be thought of in any other way but as absolute (Menger 1985, pp. 60–61).

Menger, like Mises, leaves no doubt regarding his view of the efficacy of empirically testing economic theory; providing a refutation of positivism and falsification in economics almost a century before Milton Friedman and F. A. Hayek espoused them.

Among economists the opinion often prevails that the empirical laws, "because they are based on experience," offer better guarantees of truth than those results of exact research which are obtained, as is assumed, only deductively from a priori axioms.

The error at the basis of this view is caused by the failure to recognize the nature of the exact orientation of theoretical research, of its relationship to the realistic, and by applying the points of view of the latter to the former.

Nothing is so certain as that the results of the exact orientation of

theoretical research appear insufficient and unempirical in the field of economy just as in all the other realms of the world of phenomena, when measured by the standard of realism. This is, however, self-evident, since the results of exact research, and indeed in all realms of the world of phenomena, are true only with certain presuppositions, with presuppositions which in reality do not always apply. Testing exact theory of economy by the full empirical method is simply a methodological absurdity, a failure to recognize the bases and presuppositions of exact research. At the same time it is a failure to recognize the particular aims which the exact sciences serve. To want to test the pure theory of economy by experience in its full reality is a process analogous to that of the mathematician who wants to correct the principles of geometry by measuring real objects, without reflecting that the latter are indeed not identical with the magnitudes which pure geometry presumes or that every measurement of necessity implies elements of inexactitude. Realism in theoretical research is not something higher than exact orientation, but something different.

The results of realistic orientation stand in an essentially different relationship to the empirical method than those of exact research. The former are based, of course, on the observation of phenomena in their "empirical reality" and complexity, and of course the criterion of their truth is accordingly the empirical method. An empirical law lacks the guarantee of absolute validity *a priori*, i.e., simply according to its methodological presuppositions. It states certain regularities in the succession and coexistence of phenomena which are by no means necessarily absolute. But bearing this firmly in mind, we note that it must agree with full empirical reality, from the consideration of which it was obtained. To want to transfer this principle to the results of exact research is, however, an absurdity, a failure to recognize the important difference between exact and realistic research. To combat this is the chief task of the preceding investigations (Menger 1985, pp. 69–70).

While referring to the German historical school, Menger also refuted the modern hermeneutic economists.

There is scarcely any need to remark that the nature and significance of the exact orientation of research is completely misunderstood in the modern literature on national economy. In German economics, at least in the historical school, the art of abstract thinking, no matter how greatly distinguished by depth and originality and no matter how broadly supported empirically—in brief, everything that in other theoretical sciences establishes the greatest fame of scholars is still considered, along with the products of compilatory diligence, as something secondary, almost as a stigma. The power of truth, however, will finally also be tested for those who, sensing their inability to solve the highest problems of the social sciences, would like to raise their own inadequacy as a standard for the value of scientific work in general (Menger 1985, p. 65).

Neither Hayek, who has come to accept the empirical method of Karl Popper, nor the modern hermeneuticians who advance the epistemology of subjective interpretation, have any grounding in Menger. Only Mises has accepted Menger's basic deductive procedure and forged ahead to refine it into praxeology. Mises is the true heir of the Austrian tradition and the person who has advanced the edifice of absolute economic laws in this century.

Hayek versus Menger

As Hayek progressively left his grounding in the praxeological method, he drifted further and further into error. This process has culminated in Hayek's latest work on socialism which he claims is based on Menger:

But to me, at any rate, [*Investigations*'] main interest to the economist in our days seems to lie in the extraordinary insight into the nature of social phenomena which is revealed incidentally in the discussion of problems mentioned to exemplify different methods of approach . . . Discussions of somewhat obsolete views, as that of the organic or perhaps better physiological interpretation of social phenomena, gave him an opportunity for an elucidation of the origin and character of social institutions which might, with advantage, be read by present-day economists and sociologists (Hayek 1976, p. 23).

Menger was the only one of these to have come after Darwin, yet all attempted to provide a rational reconstruction, conjectural history, or evolutionary account of the emergence of cultural institutions (Hayek 1988, p. 70).

Adequate explanations of [the market, etc.] were disseminated . . . especially by the Austrian school following Menger, into what became known as the "subjective" or "marginal utility" revolution in economic theory. [The most elementary and important] was the discovery that economic events could not be explained by preceding events acting as determining causes that enabled these revolutionary thinkers to unify economic theory into a coherent system (Hayek 1988, p. 97).

What Menger wrote about using organic analogies in the social sciences in no way justifies Hayek's claim. Menger stated clearly that the analysis of social development must be built from individual action and that reason is the guiding force in understanding social processes.

In [the organic] category belong above all the attempts of those who think that they have solved the problem involved merely by designating as "organic" the developmental process we are discussing. The process by which social structures originate without action of the common will may well be called "organic," but it must not be believed

that even the smallest part of the noteworthy problem of the social sciences that we alluded to above has been solved by this image or by any mystic allusions attached to it (Menger 1985, p. 149).

Yet Hayek makes just such allusions when he claims that the spontaneous order of the market "forms itself" or:

The answer to [how we came to acquire the economic order of the market] is built upon the old insight, well known to economics, that our values and institutions are determined not simply by preceding causes but as part of a process of unconscious self-organisation of a structure or pattern. This is true not only of economics, but in a wide area, and is well known today in the biological sciences (Hayek 1988, p. 9).

Menger sees two mistakes made in the analysis of social processes: the mystic one mentioned above, and the view that society is a product of the "common will," i.e., created by positive legislation.

Just as meaningless is another attempt to solve the problem discussed here. I mean the theory, which has attained widespread currency, that recognizes in social institutions something *original*, that is, not something that has developed, but an *original* product of the life of the people. This theory (which, incidentally, is also applied by a few of its adherents, for whom a unified principle means more than historical truth or the logic of things, by way of a peculiar mysticism to social institutions created by positive laws) indeed avoids the error of those who reduce all institutions to acts of positive common will. Still, it obviously offers us no solution of the problem discussed here, but evades it. The origin of a phenomena is by no means explained by the assertion that it *was present from the very beginning* or that it *developed originally* (Menger 1985, p. 149).

But Hayek is reduced to such a conclusion, "Although also acclaimed as a biologist, Aristotle lacked any perception of two crucial aspects of the formation of any complex structure, namely, evolution and the self-formation of order" (Hayek 1988, p. 45). Appeals to words like evolution or self-formation are not solutions to the problems of the origin and development of social institutions. Menger clearly looked to individual action as the foundation of the solution.

Such a phenomenon must obviously have developed at some time from its simpler elements; a social phenomenon, at least in its most original form, must clearly have developed from individual factors. The view here referred to is merely an analogy between the development of social institutions and that of natural organisms which is completely worthless for the purpose of solving our problem. It states, to be sure, that institutions are unintended creations of the human mind, but not *how* they came about. These attempts at interpretation are comparable to the procedure of a natural scientist who thinks he is solving the problem of the origin of natural organisms by alluding

to their "originality," "natural growth," or their "primeval nature" (Menger 1985, p. 149).

In contrast, Hayek approvingly quotes Popper, who stated, "Cultural evolution continues genetic evolution by other means" (Hayek 1988, p. 16). He continues:

For example, by the time culture began to displace some innate modes of behavior, genetic evolution had probably also already endowed human individuals with a great variety of characteristics which were better adjusted to the many different environmental niches into which men had penetrated than those of any non-domesticated animal. . . . Among the most important of these innate characteristics which helped to displace other instincts was a great capacity for learning from one's fellows, especially by imitation (Hayek 1988, p. 18).

Menger pointed out the poverty of this line of argument:

The previous attempts to interpret the *changes* of social phenomena as "organic processes" are no less inadmissible than the above theories which aim to solve "organically" the problem of the *origin* of unintentionally created social structures. There is hardly need to remark that the changes of social phenomena cannot be interpreted in a social-pragmatic way, insofar as they are not the intended result of the agreement of members of society or of positive legislation, but are the unintended product of social development. But it is just as obvious that not even the slightest insight into the nature and the laws of the movement of social phenomena can be gained either by the mere allusion to the "organic" or the "primeval" character of the processes under discussion, nor even by mere analogies between these and the transformations to be observed in natural organisms. The worthlessness of the above orientation of research is so clear that we do not care to add anything to what we have already said (Menger 1985, p. 150).

Hayek bases his analysis on exactly these allusions and analogies:

Despite such differences, all evolution, cultural as well as biological, is a process of continuous adaptation to unforeseeable events, to contingent circumstances which could not have been forecast (Hayek 1988, p. 25).

Economics has from its origins been concerned with how an extended order of human interaction comes into existence through a process of variation, winnowing and sifting far surpassing our vision or our capacity to design. . . . We are led—for example by the pricing system in market exchange—to do things by circumstances of which we are largely unaware and which produce results that we do not intend (Hayek 1988, p. 14).

Menger rejected these mystic forces and Hayek's characterization

of individuals as mindless, passive, and ignorant:

If this significant problem of the social sciences is truly to be solved, this cannot be done by way of superficial and, for the most part, inadmissible analogies. It can be done, in any case, only by way of direct consideration of social phenomena, not "organically," "anatomically," or "physiologically," but only in a *specifically sociological* way. The road to this, however, is *theoretical* social research, the nature and main orientations of which (the exact and the empirical-realistic) we have characterized above (Menger 1985, p. 150).

Hayek relies upon evolution to explain language, law, morals, markets, and money (Hayek 1988, p. 24); in contrast Menger claims that these institutions can be understood as built upon individual action.

[These are] the unintended result of innumerable efforts of economic subjects pursuing *individual* interests. The theoretical understanding of them, the theoretical understanding of their nature and their movement can thus be attained in an exact measure only in the same way as the understanding of the above mentioned social structures. That is, it can be attained by reducing them to their elements, to the *individual* factors of their causation, and by investigating the laws by which the complicated phenomena of human economy under discussion here are built up from these elements. This, however, as scarcely needs saying, is that method which we have characterized above as the one adequate for the exact orientation of theoretical research in the realm of social phenomena in general. The methods for the exact understanding of the origin of the "organically" created social structures and those for the solution of the main problems of exact economics are by nature identical (Menger 1985, pp. 158–59).

Hayek versus Mises

Menger began to build the principles of economics from what he saw as the essence of these individual factors—the human need to satisfy material ends. From this idea of subjective value, he proceeded to derive principles of action of an isolated individual, then the more complex principles; two-person exchange (based upon mutual benefit), the social division of labor, and finally, a consistent, unified theory of price (see Menger 1976). These principles were the basis of his advocacy of laissez faire (see Rothbard 1991).

Eugen von Böhm-Bawerk, accepting Menger's methodological position, constructed the theories of advanced social production, capital and interest, and demolished the underpinnings of Marxian economics (Böhm-Bawerk 1959).

Refining and building upon this work, Mises constructed a very different picture of society's origin and development from that of Hayek (Salerno 1990). His answer to a Hayekian view of society is:

To those pretending that man would be happier if he were to renounce the use of reason and try to let himself be guided by intuition and instincts only, no other answer can be given than an analysis of the achievements of human society. In describing the genesis and working of social cooperation, economics provides all the information required for an ultimate decision between reason and unreason. If man reconsiders freeing himself from the supremacy of reason, he must know what he will have to forsake (Mises 1966, p. 91).

Mises saw society as a strategy of acting individuals in their struggle against scarcity; purposefulness is the essence of the market, not spontaneity.

Seen from the point of view of the individual, society is the great means for the attainment of all his ends (Mises 1966, p. 165).

Society is concerted action, cooperation. Society is the outcome of conscious and purposeful behavior. This does not mean that individuals have concluded contracts by virtue of which they have founded human society. The actions which have brought about social cooperation and daily bring it about anew do not aim at anything else than cooperation and coadjuvancy with others for the attainment of definite singular ends. The total complex of the mutual relations created by such concerted actions is called society (Mises 1966, p. 143).

For Mises the division of labor (which is predicated on the inherent differences in individuals and natural resources) is the essence of society and the linchpin of all aspects of civilization.

Society is division of labor and combination of labor (Mises 1966, p. 143).

The fundamental social phenomenon is the division of labor and its counterpart human cooperation (Mises 1966, p. 157).

The fundamental facts that brought about cooperation, society, and civilization and transformed the animal man into a human being are the facts that work performed under the division of labor is more productive than isolated work and that man's reason is capable of recognizing this truth. But for these facts men would have forever remained deadly foes of one another, irreconcilable rivals in their endeavors to secure a portion of the scarce supply of means of sustenance provided by nature (Mises 1966, p. 144).

The law of association makes us comprehend the tendencies which resulted in the progressive intensification of human cooperation. We conceive what incentive induced people not to consider themselves simply as rivals in a struggle for the appropriation of the limited supply of means of subsistence made available by nature. We realize what has impelled them and permanently impels them to consort with one another for the sake of cooperation. Every step forward on the way to a more developed mode of the division of labor serves the

interests of all participants. In order to comprehend why man did not remain solitary, searching like the animals for food and shelter for himself only and at most also for his consort and his helpless infants, we do not need to have recourse to a miraculous interference of the Deity or to the empty hypostasis of an innate urge toward association. Neither are we forced to assume that the isolated individuals or primitive hordes one day pledged themselves by a contract to establish social bonds. The factor that brought about primitive society and daily works toward its progressive intensification is human action that is animated by the insight into the higher productivity of labor achieved under the division of labor (Mises 1966, p. 160).

The degree to which individuals extend and intensify the division of labor depends on their understanding and acceptance of it. In contrast to Hayek, who says, "The curious task of economics is to demonstrate to men how little they really know about what they imagine they can design" (Hayek 1988, p. 76), Mises attached an important role to teaching people economic principles and persuading them to pursue their "rightly understood interests."

The principle of the division of labor is one of the great basic principles of cosmic becoming and evolutionary change. The biologists were right in borrowing the concept of the division of labor from social philosophy and in adapting it to their field of investigation . . . But one must never forget that the characteristic feature of human society is purposeful cooperation; society is an outcome of human action, i.e., of a conscious aiming at the attainment of ends. No such element is present, as far as we can ascertain, in the processes which have resulted in the emergence of the structure-function-systems of plant and animal bodies and in the operation of the societies of ants, bees, and hornets. Human society is an intellectual and spiritual phenomenon. It is the outcome of a purposeful utilization of a universal law determining cosmic becoming, viz., the higher productivity of the division of labor. As with every instance of action, the recognition of the laws of nature is put into the service of man's efforts to improve his conditions (Mises 1966, p. 145).

The body of economic knowledge is an essential element in the structure of human civilization; it is the foundation upon which modern industrialism and all the moral, intellectual, technological, and therapeutical achievements of the last centuries have been built. It rests with men whether they will make the proper use of the rich treasure with which this knowledge provides them or whether they will leave it unused. But if they fail to take the best advantage of it and disregard its teachings and warnings, they will not annul economics; they will stamp out society and the human race (Mises 1966, p. 885).

The prerequisite for advanced social production is calculation that allows purposeful action within the framework of the division of

labor. Calculation requires money prices and thus, money and free exchange, which requires private property.

Economic calculation is the fundamental issue in the comprehension of all problems commonly called economic (Mises 1966, p. 199).

Monetary calculation is the guiding star of action under the social system of division of labor. It is the compass of the man embarking upon production.

The system of economic calculation in monetary terms is conditioned by certain social institutions. It can operate only in an institutional setting of the division of labor and private ownership of the means of production in which goods and services of all orders are bought and sold against a generally used medium of exchange, i.e., money.

Monetary calculation is the main vehicle of planning and acting in the social setting of a society of free enterprise directed and controlled by the market and its prices.

Our civilization is inseparably linked with our methods of economic calculation. It would perish if we were to abandon this most precious intellectual tool of action (Mises 1966, pp. 229–30).

From this analysis Mises made his criticism of socialism, that it cannot calculate and thus, it is not an *economic* system at all. The attempt to implement socialism must lead to poverty, death, and retrogression of civilization. Mises said, "In abolishing economic calculation the general adoption of socialism would result in complete chaos and the disintegration of social cooperation under the division of labor" (Mises 1966, p. 861). While Mises saw calculation as *the* problem of socialism, Hayek views it as a knowledge problem:

To the naive mind that can conceive of order only as the product of deliberate arrangement, it may seem absurd that in complex conditions order, and adaptation to the unknown, can be achieved more effectively by decentralizing decisions, and that a division of authority will actually extend the possibility of overall order. Yet that decentralization actually leads to more information being taken into account. This is the main reason for rejecting the requirements of constructivist rationalism (Hayek 1988, pp. 76–77).

Mises demonstrated that even with *perfect* information, the central planners in socialism cannot rationally calculate how to combine resources to render efficient production (Ebeling 1991). They can only grope in the dark; as Mises put it, socialism is "planned chaos," an irrational endeavor that must leach off and mimic capitalism to provide even a subsistence standard of living to its citizens.

The paradox of "planning" is that it cannot plan, because of the absence of economic calculation. What is called a planned economy is no economy at all. It is just a system of groping about in the dark. There is no question of a rational choice of means for the best possible attainment of the ultimate ends sought. What is called conscious planning is precisely the elimination of conscious purposive action (Mises 1966, pp. 700–01).

If no other objections could be raised to the socialist plans than that socialism will lower the standard of living of all or at least of the immense majority, it would be impossible for praxeology to pronounce a final judgment. Men would have to decide the issue between capitalism and socialism on the ground of judgments of value and of judgments of relevance. . . . However, the true state of affairs is entirely different. Man is not in a position to choose between these two systems. Human cooperation under the system of the social division of labor is possible only in the market economy. Socialism is not a realizable system of society's economic organization because it lacks any method of economic calculation (Mises 1966, p. 679).

Mises and the Austrian Tradition

These principles, representing the pinnacle of free-market economic theory, cannot be found in any other modern school of economic thought. By failing to correctly understand the process of the social creation of wealth these other schools have not played a significant, independent role in the current advancement of freedom. Advocates of the free market within other schools have relied upon the basic Austrian arguments or have been relatively ineffective since their economic theories are more easily rebuffed.

What effective defense of the free market has been made by econometrics? By its nature all such work tells us only of what has happened and not what can happen—it cannot result in universal laws applicable to any conceivable historical episode. As such it is easily ignored by those who wish to conduct social experiments for the future. Furthermore, econometrics is coming under increasing criticism as a method capable of rendering useful knowledge at all (see Hoppe 1988).

This criticism extends with equal force to modern neoclassical theory, since it is built upon positivism (Friedman 1974). Milton Friedman tells us that all proper economic theory must be testable and subject to falsification; that economic propositions, like those in physics, are hypothetical, tentative, and forever subject to testing and potential rejection. Yet what basic principles of economics have neoclassical economists rejected for failing tests of statistical significance? The laws of supply and demand? The principle of diminishing marginal utility? The concept of opportunity cost? The idea that exchange leads to

mutual benefit? Such basic principles are either non-testable, and thus, not positivist economic theories at all, or routinely rejected in econometric tests. Yet all *economic* defenses of the free market are built from basic principles. Friedman and other neoclassical economists say that economic theory must be empirical but they do economic theory deductively, although not as well as Mises.

Neoclassical economics has failed to provide any role in defense of the free market to the extent that it stands outside the Austrian tradition. It contains no free-market principles that are both unique and true. It should be kept in mind that after Mises's devastating article on the inability of socialism to calculate, socialists tried to refute him by using mathematical economics and econometrics to show that, in theory at least, the problem could be solved by a system of equations *if* the economy is perfectly competitive (Ebeling 1991). Their failure has not prevented others from employing the pre-eminent neoclassical theory as an argument *against* the free market. It is a common barb that the free market would be a superior economic system *if* it was perfectly competitive. And since it obviously is not perfectly competitive, then government control is essential.

To the contrary, Mises has shown that the argument for free markets does not depend on *any* type of competition, perfect or otherwise. In contrast, Hayek claims:

One revealing mark of how poorly the ordering principle of the market is understood is the common notion that "cooperation is better than competition." Cooperation, like solidarity, presupposes a large measure of agreement on ends as well as on methods employed in their pursuit. It makes sense in a small group whose members share particular habits, knowledge and beliefs about possibilities. It makes hardly any sense when the problem is to adapt to unknown circumstances; yet it is this adaptation to the unknown on which the coordination of efforts in the extended order rests. Competition is a procedure of discovery, a procedure involved in all evolution, that led man unwittingly to respond to novel situations; and through further competition, not through agreement, we gradually increase our efficiency.

To operate beneficially, competition requires that those involved observe rules rather than resort to physical force. Rules alone can unite an extended order. Neither all ends pursued, nor all means used, are known or need to be known to anybody, in order for them to be taken account of within a spontaneous order. Such an order forms of itself (Hayek 1988, pp. 19–20).

Biological and cultural evolution share other features too. For example, they both rely on the same principle of selection: survival or reproductive advantage. Variation, adaptation and competition are essentially the same kind of process, however different their particular

mechanisms, particularly those pertaining to propagation. Not only does all evolution rest on competition; continuing competition is necessary even to preserve existing achievements (Hayek 1988, p. 26).

Mises has shown that the social division of labor is not an arena of competition but cooperation, a complex network of voluntary interaction that is absolutely necessary for the continuing life and prosperity of the world's population. If people fail to understand this and act against their "rightly understood interests" then prosperity and civilization will end.

What makes friendly relations between human beings possible is the higher productivity of the division of labor. It removes the natural conflict of interests. For where there is division of labor, there is no longer question of the distribution of a supply not capable of enlargement. Thanks to the higher productivity of labor performed under the division of tasks, the supply of goods multiplies. A pre-eminent common interest, the preservation and further intensification of social cooperation, becomes paramount and obliterates all essential collisions. Catallactic competition is substituted for biological competition. It makes for harmony of the interests of all members of society. The very condition from which the irreconcilable conflicts of biological competition arise—viz., the fact that all people by and large strive after the same things—is transformed into a factor making for harmony of interests. Because many people or even all people want bread, clothes, shoes, and cars, large-scale production of these goods becomes feasible and reduces the costs of production to such an extent that they are accessible at low prices. The fact that my fellow man wants to acquire shoes as I do, does not make it harder for me to get shoes, but easier. What enhances the price of shoes is the fact that nature does not provide a more ample supply of leather and other raw material required, and that one must submit to the disutility of labor in order to transform these raw materials into shoes. The catallactic competition of those who, like me, are eager to have shoes makes shoes cheaper, not more expensive.

This is the meaning of the theorem of the harmony of the rightly understood interests of all members of the market society (Mises 1966, pp. 673–74).

Most "free-market" economists have failed to absorb Mises's analysis of capitalism and socialism and thus hold to some form of a mixed economy. As Mises has shown this view is untenable.

The market economy must be strictly differentiated from the second thinkable—although not realizable—system of social cooperation under the division of labor: the system of social or governmental ownership of the means of production. This second system is commonly called socialism, communism, planned economy, or state capitalism. The market economy or capitalism, as it is usually called,

and the socialist economy preclude one another. There is no mixture of the two systems possible or thinkable; there is no such thing as a mixed economy, a system that would be in part capitalistic and in part socialist. Production is directed by the market or by the decrees of a production tsar or a committee of production tsars.

If within a society based on private ownership by the means of production some of these means are publicly owned and operated—that is, owned and operated by the government or one of its agencies—this does not make for a mixed system which would combine socialism and capitalism. . . . These publicly owned and operated enterprises are subject to the sovereignty of the market. They must fit themselves, as buyers of raw materials, equipment, and labor, and as sellers of goods and services, into the scheme of the market economy. They are subject to the laws of the market and thereby depend on the consumers who may or may not patronize them. They must strive for profits or, at least, to avoid losses. The government may cover losses of its plants or shops by drawing on public funds. But this neither eliminates nor mitigates the supremacy of the market; it merely shifts it to another sector.

Nothing that is in any way connected with the operation of a market is in the praxeological or economic sense to be called socialism. The notion of socialism as conceived and defined by all socialists implies the absence of a market for factors of production and of prices of such factors. The “socialization” of individual plants, shops, and farms—that is, their transfer from private into public ownership—is a method of bringing about socialism by successive measures. It is a step on the way toward socialism, but not in itself socialism (Mises 1966, pp. 258–59).

This step-by-step process, in reverse, is the council given to the countries of Eastern and Central Europe by today’s self-proclaimed, free-market economists. After moving toward capitalism, they are to stop at some optimum amount of government intervention. But Mises showed long ago that interventionism is an unstable middle ground between capitalism and socialism that must continue in motion toward one or the other.

The system of interventionism or of the hampered market economy differs from the German pattern of socialism by the very fact that it is still a market economy. The authority interferes with the operation of the market economy, but does not want to eliminate the market altogether. It wants production and consumption to develop along lines different from those prescribed by an unhampered market, and it wants to achieve its aim by injecting into the working of the market orders, commands, and prohibitions for whose enforcement the police power and its apparatus of violent compulsion and coercion stand ready. But these are *isolated* acts of an integrated system which determines all

prices, wages and interest rates and thus places full control of production and consumption into the hands of the authorities.

The system of the hampered market economy or interventionism aims at preserving the dualism of the distinct spheres of government activities on the one hand and economic freedom under the market system on the other hand. What characterizes it as such is the fact that the government does not limit its activities to the preservation of private ownership of the means of production and its protection against violent or fraudulent encroachments. The government interferes with the operation of business by means of orders and prohibitions (Mises 1966, p. 718).

The interventionist doctrinaires repeat again and again that they do not plan the abolition of private ownership of the means of production, of entrepreneurial activities, and or market exchange. . . . It is necessary, they say, that the state interfere with the market phenomena whenever and wherever the "free play of the economic forces" results in conditions that appear as "socially" undesirable. In making this assertion they take it for granted that it is the government that is called upon to determine in every single case whether or not a definite economic fact is to be considered as reprehensible for the "social" point of view and, consequently whether or not the state of the market requires a special act of government interference.

All these champions of interventionism fail to realize that their program thus implies the establishment of full government supremacy in all economic matters and ultimately brings about a state of affairs that does not differ from what is called the German or the Hindenburg pattern of socialism. If it is in the jurisdiction of the government to decide whether or not definite conditions of the economy justify its intervention, no sphere of operation is left to the market. Then it is no longer the consumers who ultimately determine what should be produced, in what quantity, of what quality, by whom, where, and how—but it is the government. For as soon as the outcome brought about by the operation of the unhampered market differs from what the authorities consider "socially" desirable, the government interferes. That means the market is free as long as it does precisely what the government wants it to do. . . . Thus the doctrine and the practice of interventionism ultimately tend to abandon what originally distinguished them from outright socialism and to adopt entirely the principles of totalitarian all-round planning (Mises 1966, pp. 723–24).

In Mises's view what we are witnessing today is not the collapse of socialism, since socialism cannot be realized in full, but the collapse of a form of interventionism. He predicted this in 1949: "The interventionist interlude must come to an end because interventionism cannot lead to a permanent system of social organization" (Mises 1966, p. 858). This must happen because interventionism restricts

the goods available to consumers; and fails to bring about the end aimed at, leading to a situation worse than the pre-intervention once it has exhausted the “surplus” it seeks to confiscate (Mises 1966, p. 858). The outcome of changes in Europe depend upon understanding and accepting these Misesian ideas.

Optimists hope that at least those nations which have in the past developed the capitalist market economy and its civilization will cling to this system in the future too. There are certainly as many signs to confirm as to disprove such an expectation. It is vain to speculate about the outcome of the great ideological conflict between the principles of private ownership and public ownership, of individualism and totalitarianism, of freedom and authoritarian regimentation. All that we can know beforehand about the result of this struggle can be condensed in the following three statements:

- (1) We have no knowledge whatever about the existence and operation of agencies which would bestow final victory in this clash on those ideologies whose application will secure the preservation and further intensification of societal bonds and the improvement of mankind's material well-being. Nothing suggests the belief that progress toward more satisfactory conditions is inevitable or a relapse into very unsatisfactory conditions impossible.
- (2) Men must choose between the market economy and socialism. They cannot evade deciding between these alternatives by adopting a “middle-of-the-road” position, whatever name they may give to it.
- (3) In abolishing economic calculation the general adoption of socialism would result in complete chaos and the disintegration of social cooperation under the division of labor (Mises 1966, p. 861).

We are all participating in this great ideological struggle and thus economic education holds paramount importance.

Economics must not be relegated to classrooms and statistical offices and must not be left to exoteric circles. It is the philosophy of human life and action and concerns everybody and everything. It is the pith of civilization and of man's human existence.

There is no means by which anyone can evade his personal responsibility. Whoever neglects to examine to the best of his abilities all the problems involved voluntarily surrenders his birthright to a self-appointed elite of supermen. In such vital matters blind reliance upon “experts” and uncritical acceptance of popular catchwords and prejudices is tantamount to the abandonment of self-determination and to yielding to other people's domination. As conditions are today, nothing can be more important to every intelligent man than economics. His own fate and that of his progeny is at stake (Mises 1966, p. 878).

Conclusions

The Austrian tradition is identified by and built upon praxeology—the application of deductive reasoning to the irrefutable fact of human action. This method is the red thread that runs from Menger to Böhm-Bawerk to Mises to Murray Rothbard and the modern practitioners of Austrian economics. Working within this tradition, economists have produced a great edifice of irrefutable, universally applicable economic theory. They have shown how the free market advances mankind in its struggle against scarcity and why socialism cannot do so. They have taught us that we must choose one of these two social arrangements, since no system exists between them. We must make our selection and advance, by education and persuasion, either capitalism or socialism. Let us choose wisely.

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