

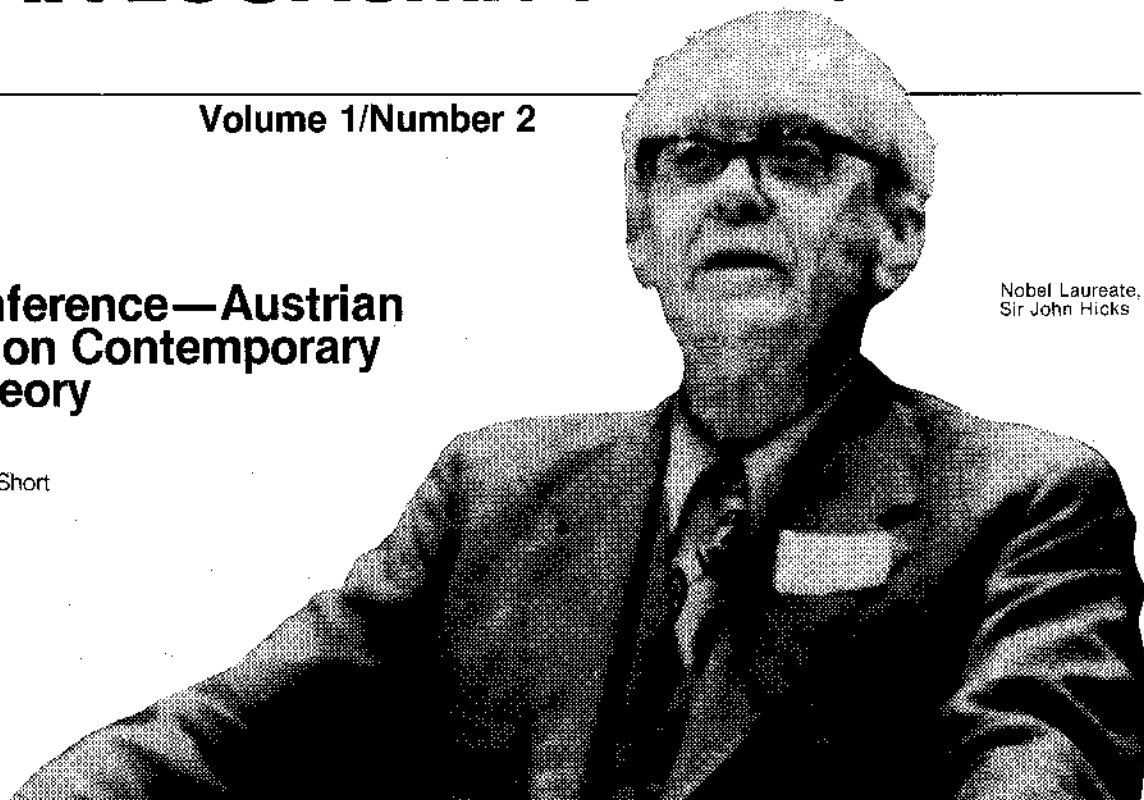
# THE AUSTRIAN ECONOMICS NEWSLETTER

Spring 1978

Volume 1/Number 2

## The NYU Conference—Austrian Perspectives on Contemporary Economic Theory

by Gary G. and Eugenie D. Short



Nobel Laureate,  
Sir John Hicks

Perhaps the most successful of the recent Austrian conferences was held at New York University on Jan. 7-8, 1978. The conference, "Issues in Economic Theory: An Evaluation of Current Austrian Perspectives," was directed by Dr. Mario J. Rizzo and sponsored jointly by the Center for Applied Economics of NYU and the Institute for Humane Studies. Approximately 150 economists attended from various institutions throughout the United States as well as from Great Britain and Australia. Among those attending were the editors of three leading economic journals: *Economic Inquiry*, the *Journal of Economic Literature*, and the *Southern Economic Journal*. Sessions were held at the NYU School of Law and consisted of six papers and comments primarily examining Austrian insights into important questions confronting the economics profession.

The conference began Saturday morning with a paper by Professor Gerald P. O'Driscoll, Jr., (Iowa State) entitled "Rational Expectations, Politics, and Stagflation." O'Driscoll drew attention to a relatively neglected paradox between two widely discussed bodies of contemporary thought in economics: rational expectations and political business cycle theories. The implication of the former is that economic policy will have no real effects on the economy since individuals will anticipate policy

changes and adjust their behavior in a manner which offsets the effect of these policies while the latter theory implies that economic policy does cause real economic fluctuations.

Professor O'Driscoll argued that there are important insights in both theories, as well as errors. Providing a thorough examination of the rational expectations literature, he observed that expectations are certainly important in influencing individual behavior and hence it is desirable to see economists focusing on them. However, he criticized the existing literature for merely replacing the traditional assumption of perfect knowledge of outcomes with the no less restrictive assumption of perfect knowledge of subjective probability distributions. O'Driscoll also pointed out that the rational expectations approach is incapable of dealing with aspects of uncertainty such as "incomplete listability," i.e., a state of affairs where the agent does not know (and does not presume to know) all of the possible outcomes. In other words, the rational expectations approach cannot deal with Knightian uncertainty. Further, O'Driscoll was critical of the rational expectations theorists for neglecting F.A. Hayek's insight that monetary expectations can distort the whole structure of relative prices because of the misinformation that the price system, working

through the interest rate, can transmit in such circumstances.

Professor O'Driscoll concluded by comparing the theoretical frameworks used by the Rational Expectations and Political Business Cycle Theorists. He pointed out that the two approaches are similar in that both assume that individuals will respond to policy changes in a "rational" manner. However, the implications derived from these two approaches are quite different since "rational behavior" is interpreted in two rather distinct ways.

Commenting on the O'Driscoll paper was Professor Richard Wagner of VPI, who insisted that the only difficulty with the paper was that it did not go far enough. Drawing from his own work on Political Business Cycle theory, Wagner argued that rather than being primarily concerned with the impact of policy on macro-aggregates, the intent of political action is to influence the state of variables affecting *particular individuals* with aggregate consequences emerging only as a by-product. Working within a public choice framework, Wagner asserted that the motivating factor behind the monetary authorities decision to print money is that some groups are able to profit from inflationary policies and these groups provide incentives for the authorities to pursue this course of action.

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# Austrian Economics Seminar, Part I: 1975-76

by Don C. Lavoie

## AUSTRIAN ECONOMICS NEWSLETTER

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The *Austrian Economics Newsletter* is designed as a research and communications device for work in Austrian economics. As such, it is essential that we have the active support and cooperation of our readers. We need any information which would be of value to other Austrians and we welcome any suggestions for improving the *Newsletter*. The success of the *Newsletter* fundamentally depends on our ability to encourage the participation and involvement of our readers.

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When the last of Ludwig von Mises' regular seminars in Austrian economics ended at NYU in 1969, it looked like the last dying gasp of the Austrian school. Ludwig Lachmann had said he expected that when Hayek died he would be the last living expositor of this once widely held point of view. But the resurgence of Austrian economics in the 1970's has exceeded the expectations of even the most optimistic among us. In a series of conferences beginning with South Royalton a whole host of young enthusiasts of modern subjectivism were discovered. And in September, 1975, only six years after Mises' seminar ended, the new Austrian Economics Seminar was formed.

This was the result of the efforts of Professor Walter Block who circulated a letter to some of the prominent exponents of the modern Austrian school living in the New York City area (Professors Grinder, Kirzner, Lachmann, Rothbard and Spadaro) suggesting the formation of a monthly seminar and outlining a possible format. The main purposes outlined were that the Austrian Economics Seminar (AES) serve as an advanced seminar extending the frontier of Austrian economics, and as a vehicle for the criticism and improvement of new Austrian contributions.

These expectations were remarkably well confirmed by the ensuing operation of the AES. Genuine and significant contributions to economics have been forged by some of the papers, but it has been the actual two-hour discussions among the leading luminaries of Austrian economics that have proved invaluable. For the first time, two of the most prominent American students of Mises—Murray Rothbard and Israel Kirzner—engaged in controversial discussions with such perceptive Austrian economists as Ludwig Lachmann, Walter Grinder and others. It proved to be a veritable feast of knowledge for those whose intellectual appetites have been stimulated by the various writings of these scholars. The many points of contention among the different participants were brought into sharper focus and the various strands and tendencies of Austrian economics were more clearly identified during these animated discussions than had heretofore been the case. Until recently Austrian economics had often matured independently in the minds of isolated readers, taking on different shades of emphasis and interpretation which had not had much chance for confrontation in the fruitful atmos-

phere of scientific criticism. It was in the AES that the Austrian spectrum was revealed and the lines of disagreement drawn. Rothbard and others attacked what has affectionately come to be known as "Lachmannia," an allegedly nihilistic tendency associated with Keynes and Shackle. On the other hand, Lachmann and others attacked what they perceived as latent "Ricardianism", a mechanistic tendency allegedly implicit in some of the Austrian literature.

Indeed much of the argumentative history of the AES can be analyzed as a gradual recognition of these two poles of thought, and the clarification or resolution of points of dispute between them. On the one hand, if we treat expectations as entirely autonomous then the future becomes unknowable and it seems that economics can say nothing at all. On the other hand, we cannot be satisfied with mechanistic economic reasoning where events are completely determinate and it seems that economics claims too much.

The "nihilistic" extreme at times appears to discard equilibrium analysis simply because we are never in equilibrium, stressing the diversity of expectations and seeing the market as including both equilibrating and disequilibrating forces. In contrast, the "Ricardian" extreme seems to ignore disequilibrating elements, stressing the market process whereby plans are made more convergent with each other. As in any advanced discussion much effort is required just to understand what each contributor is trying to say, and these "poles" of thought are frequently found to represent only matters of different emphasis.

The first meeting of the AES was held at New York University on December 17, 1975, to discuss Professor Joseph Salerno's "The Modern Monetary Theory of the Balance of Payments: A Subjectivist Critique". There were three major foci of discussion: methodology, the Evenly Rotating Economy and the Keynesian tripartite division of the demand for money. The methodological issue arose in response to Salerno's heavy emphasis on method, given an economic academia in which fundamental methodological questions are rarely asked. Austrians were urged to take pains to show how and where our approach would yield significantly different conclusions. We will be heeded as a scientific school only to the extent

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## Gerald P. O'Driscoll, Jr.

### *Economics as a Coordination Problem: The Contributions of*

*Friedrich A. Hayek.* Sheed Andrews and McMeel, xxi, 240 pp. \$12.00, pb \$4.95

Reviewed by Jeffrey Rogers Hummel

Of the writings of all Austrian economists, those of Friedrich Hayek are undoubtedly the most difficult, complex, even obscure. Any effort, therefore, to explicate them or make them more readily understandable to a wider audience provides a valuable service. Gerald O'Driscoll's first book, *Economics as a Coordination Problem*, is such an effort and, for that reason alone, deserves to be applauded. Furthermore, O'Driscoll has gone beyond a mere summary of Hayek's ideas; he has identified the fundamental theme that integrates and ties together all of Hayek's positions but that Hayek himself never made explicit. Showing how Hayek's treatment of each specific issue is simply another illustration of the coordination problem, which in turn is the central question for the discipline of economics, is a flash of insight from which many students of Austrian economics have profited already.

Unfortunately, *Economics as a Coordination Problem* is also a flawed book with several drawbacks, two of which I will consider. First, while O'Driscoll includes extensive, explicit treatment of most of Hayek's works, especially of *Prices and Production* and *Profits, Interest and Investment*, he all but ignores *The Pure Theory of Capital*. O'Driscoll only mentions *The Pure Theory of Capital* about five times in the entire book, and this despite the fact that one of those times is to refer to it as Hayek's *magnum opus*. In fact, *The Pure Theory of Capital* is Hayek's most difficult work, the one most in need of elucidation. If Hayek's other books deserve a full treatment, then surely it does.

A second flaw in O'Driscoll's book is, in my opinion, more serious, and it stems partially from the first. O'Driscoll, in a series of chapters that successively build upon one another, gives Hayek's approach to issues of increasing complexity until reaching the final issue: business cycles. While discussing this final issue, O'Driscoll treats the title essay of Hayek's *Profit, Interest and Investment* as the most advanced statement of Hayek's business cycle theory. This sequence, in effect, represents *Profits, Interest and Investment* as the culmination of Hayek's thought.

This is a peculiar way to view *Profits, Interest and Investment* for three reasons. To begin with, Hayek conducts the analysis in that book within the context of four very restrictive and far-reaching, though usually unrealistic

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Reviewed by Richard M. Ebeling

When studying social phenomena, it is necessary to remember that all man-made objects and recorded data of prices and quantities are merely the historical sediments of previous human plans. To successfully understand the relationships between those objects, quantities and prices it is incumbent upon the social scientist to analyze the ends and means of the human actors involved. If we are to know what things mean in the social world we must try to understand what the purposeful acting agents meant.

The task is the same—and no less difficult—when it involves the analysis of an author's work. To successfully capture another person's perspective as presented through his written words is a notable achievement. This is what makes Dr. Gerald P. O'Driscoll's book, *Economics as a Coordination Problem: The Contributions of Friedrich A. Hayek*, such a valuable addition to the bookshelf of Austrian literature.

Dr. O'Driscoll has brought together the various strands of thought developed by Friedrich A. Hayek and has demonstrated the underlying theme in all of them. In the forward, Professor Hayek admits that he "was occasionally . . . surprised when I found in professor O'Driscoll's account side by side statements I made at the interval of many years on quite different problems, which still implied the same general approach."

The underlying theme that O'Driscoll has seen in Hayek's work concerns an understanding and appreciation of how, in a world of imperfect knowledge, the divergent plans of a multitude of individuals are brought into consistency in the market economy.

Existing general-equilibrium theory guarantees the consistency of plans by postulating a set of conditions that makes anything less impossible. It has never fully explained how those conditions could be expected to exist in a real market or what forces could be expected to propel the economy towards the equilibrium solution.

As Dr. O'Driscoll explains, Hayek was interested in analyzing both the institutional arrangements under which coordination could be brought about and the nature of the process involved. It was the price system as a transmitter of information that Hayek came to see as the focal point of this process.

In the three central chapters of the book, O'Driscoll provides an extremely

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## The NYU Conference— Austrian Perspectives on Contemporary Economic Theory (Continued)

Conference director Mario Rizzo presented the second paper, "Uncertainty, Subjectivity and the Economic Analysis of the Law." Dr. Rizzo examined the now popular contention in much of the law and economics literature that the law of torts promotes economic efficiency. He demonstrated that there are serious difficulties understanding the meaning of this contention since "efficiency" is either irrelevant to the economic agents or it is a tautology since every situation will be seen to be efficient, if all relevant constraints are recognized. Additionally, Rizzo examined six major legal precedent areas which appear to contradict the assertion that the law of torts promotes efficiency. Finally, he presented the position that outside of general competitive equilibrium, the minimization of objectively measurable costs does not ensure the minimization of true social opportunity costs. Therefore, even if it were possible to show that tort law minimizes the former, (which he argues it does not), it would still not follow that it minimizes the latter.

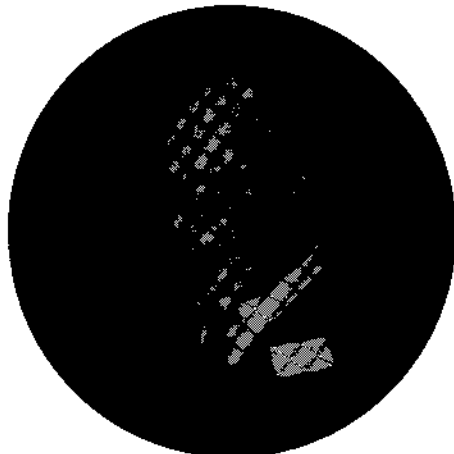
Professor Murray N. Rothbard of the New York Polytechnic Institute commented on Dr. Rizzo's paper. He voiced his wide agreement with the paper and stressed the meaninglessness of the concept of economic efficiency. Following Rothbard's comments a lively discussion from the audience ensued. Harold Demsetz, from UCLA, took Rizzo to task for the view that six cases were enough to counter the vast empirical research of Posner, Landes, and others which supports the hypothesis that tort law does promote efficiency. Rizzo responded that the cases discussed in his paper were important legal precedents which show that in significant areas the law of torts clearly does not promote efficiency.

Nobel Laureate Sir John Hicks presented Saturday's final paper, "Is Interest the Price of a Factor of Production?" His remarks were wide ranging and only in the second half of the paper did he address his title question, answering it in the affirmative. Throughout the first half of his paper Sir John chided the Austrians for their excessive mistrust of the notion of equilibrium, accusing them of rejecting equilibrium analysis "even as a tool of analysis." However, Hicks himself admitted to having become "quite critical of equilibrium economics"—at least of the manner in which it is often utilized.

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## The NYU Conference— Austrian Perspectives on Contemporary Economic Theory (Continued)

Ludwig Lachmann, visiting professor at NYU commented on Sir John's paper. In his comment Lachmann stated that there is much common ground between Hicks and the Austrians although "the sources of our disagreements run rather deep." Lachmann explained that Austrians do not object to the concept of equilibrium *per se*, particularly indivi-



Professor Ludwig Lachman

dual equilibrium (self-consistent action), or Marshallian partial equilibrium. They do, however, object to the general equilibrium models of Walras and Pareto. Lachmann further contended that there is more to economics than determinate models and that "human action, in its more interesting forms, cannot be pressed into this mold without losing most of its distinguishing characteristics."

Following the discussion of the Hicks' paper, a cocktail party and banquet was held. After dinner Professor Israel Kirzner of NYU gave a warm and inspiring tribute to Professor Lachmann, honoring him for his contributions to Austrian economics and to the NYU program. (Professor and Mrs. Lachmann have since returned to South Africa after a three year stay in the U.S.) The evening ended with Sir John toasting the health of the Austrian school.

Professor Harvey Leibenstein of Harvard opened Sunday's session with his paper, "The General X-Efficiency Paradigm and the Role of the Entrepreneur." He briefly outlined his work on x-efficiency and then related it to the theory of entrepreneurship. Leibenstein argued that the greater the x-efficiency there is in an economy, the greater is the role for entrepreneurship. He also stressed that there is no role for the entrepreneur within a general equilibrium framework  
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## Austrian Economics Seminar, Part I: 1975-76 (Continued)

that our method can handle problems and surmount obstacles which other approaches cannot.

The Misesian imaginary construction of the Evenly Rotating Economy was the second major topic of discussion. Mises had argued that the ERE was unrealizable in the real world but was only a construct intended to explain the result of the tendency of entrepreneurial action. In the real world of change entrepreneurs must continually adjust their actions toward greater coordination, though complete coordination is never achieved. On the other hand, in a mental experiment where no other changes impinge, we can imagine complete coordination (the equilibrium state of the ERE) resulting. This issue was brought up in relation to Mises' argument that in the ERE the demand for money would fall to zero since money is only useful in a world of uncertainty, and thus prices would rise to infinity and the market process would end. Some participants argued that in approaching such a world another commodity, for example some readily accessible form of credit, would become the most marketable commodity and accounting prices could still be used in non-money units. It was widely agreed that the usefulness of the mental construct does not depend on its realizability.

This discussion led to a third issue, the Keynesian tripartite division of the demand for money into transactions, speculative and precautionary demand. A strong objection to these categories was that they overlap. Since a transactions demand is for an uncertain future, it must have both precautionary and speculative motivations inextricably bound up in it. In principle the economist may analyze hypothetical cases where a particular motivation is dominant. However, such an investigation might more appropriately be classified as market research, analogous to discovering the inner motivations of a peanut consumer, rather than as economic theory *per se*. A recurring theme of AES discussions has been the dispute over the scope of economic theory. The praxeological view of economics as the logic of action recognizes psychology and history as separate disciplines. In contrast much of modern economics has tended to blur psychological matters (e.g., estimations of aggregate consumer demand) and historical matters (e.g., econometric studies) with economic theory.

The second meeting of the AES (January 14, 1976) began with a discussion of the Dallas AEA sessions on the economics of F.A. Hayek. Ludwig Lachmann, one of Hayek's best students at the London School of Economics led the discussion with a summary of the proceedings. The main topic of discussion, however, was the paper: "A Theoretical and Empirical Analysis of the Spatial Diffusion of Inflation" by Murray Sabrin. A major point of Austrian monetary theory has always been that inflation will cause relative prices to change, with some prices moving before others. In a modern market economy the exact sequence of price rises (separated out from noninflationary price adjustments) is a bewilderingly complex matter. In the discussion of Sabrin's paper the main question was the interpretation to be given to the empirical data, and whether meaningful empirical results are even possible. Since markets are integrated through high speed data communications we would not expect inflation to smoothly ripple through the geographic landscape. Although one might observe prices rising earlier near the sources of new money (for example, near Federal Reserve Banks) than in the remote countryside, this need not be the case. Most participants concurred that this empirical work would at best illustrate and not test Austrian inflation theory. The possibility of measuring Hayekian distortions in the capital structure (resulting from credit expansion) was also raised. Would one find capital goods prices in general rising in advance of consumer goods prices? That the industrial commodities index is not disaggregated by regions (in contrast to the CPI) makes such empirical study difficult at present. The possibility of applying Leontief's Input/Output empirical studies to Hayekian cycle theory was also considered.

The third meeting of the AES, held on February 17, 1976, discussed Walter Grinder's "An Investigation into the Problem of Misinvestment and Capital Distortion Concerning Subsidization of Research and Development", a prospectus for an (unsubsidized) research project. His intention was to "clarify theoretically and to illustrate empirically why 'Austrians' are certain that government subsidization of public or private R and D will very likely lead to a misallocation of resources, a distortion of the structure of production, and will  
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# Methodology Conference Held at University of Delaware

by John Kunze

To promote scholarly methods in social research, the Institute for Humane Studies recently sponsored a Symposium on Methodology in the Social Sciences at the University of Delaware. The conference was well organized by Leonard Liggio (Cato Institute) and graciously hosted by Burton Abrams (Economics; University of Delaware). About thirty-five scholars attended the four day conference (November 19-23). Participants represented such disciplines as philosophy, history, law, political science and sociology, but two thirds were economists. Likewise, half of the papers dealt with economics. The papers were distributed well in advance of the conference and this procedure greatly facilitated discussion. Indeed most scholarly discussions are more successful if the participants are familiar with the particular positions being considered.

Since conferees had already read the papers, each session began with prepared comments by the senior commentators who included Professors Neil B. De Marchi (Economics; Duke), J. Charles King (Philosophy; Pomona College), Israel M. Kirzner (Economics; NYU), Ludwig M. Lachmann (Economics; NYU), Louis M. Spadaro (Economics; Fordham), Vincent J. Tarascio (Economics; University of North Carolina) and Leonard Liggio.

Although the quality of the papers varied, each stimulated interesting discussion. Indeed this was their most valuable service. By dealing with controversial questions, they encouraged an appreciation of the complexity of the problems which must be solved.

The majority of the papers considered either the Austrian contribution to the methodology of economics, the debate on the growth of knowledge literature (Popper, Kuhn, Lakatos and others) or both. Since most conferees were familiar with these topics, the discussion proved to be progressive with arguments expressed in one session setting the stage for higher level discussion in later sessions.

The first paper considered was Samuel Bostaph's (Economics; Western Maryland College) "On the Origin of Methodological Differences Among Economists and the Resolution of the Resulting Conflicts over Methods." He argued that methodological disputes result from epistemological and metaphysical questions and developed a methodological position from a metaphysical assumption of the law of causality, and

the Objectivist theory of concepts. Criticizing the Humean view of causality, he distinguished between two types of causality, the mechanistic causality of the natural world and the teleological causality of the social world. Thus he concluded the methods of the two disciplines may be expected to differ.

Robert Bradley, Jr., (Economics, University of Houston) provided the second paper: "Positivism and Praxeology: An Essay on the Philosophy of Economics." Bradley provided a thorough survey of the Austrian criticism of positivism and contrasted it with praxeology. He concluded with an examination and defense of the Austrian approach.

Mario Rizzo's (Economics; NYU) "Equilibrium and Optimality: A Methodological Investigation" explored the relationship between equilibrium and optimality to determine the value of each concept. He argued that any situation could be analyzed as a relevantly restricted equilibrium (given transactions costs, the distribution of knowledge and other relevant constraints) and thus as an equally restricted optimum. Since in this sense all situations are optimal, Rizzo questioned the usefulness of optimality as a concept. He then identified situations which, though consistent with a maximization framework, could be more fruitfully analyzed from other perspectives. He concluded by noting that only the introduction of value judgements would give "optimality" content not shared by "equilibrium."

The first session on Monday considered David M. Levy's (National Planning Association) paper, "'False' Theorems or 'Mistaken' Choices in the Study of Human Action." Levy drew on the ideas of Mises, George Stigler and Gary Becker ("De Gustibus Non Est Disputandum," *AER*, March, 1977), John Locke, and Bernard Mandeville to explore the problems which "arise for a theory of choice which allows individuals to to make 'mistakes'." He concluded that the concept "mistake" is useful only when defined ex post in a means-end framework. An "ex ante mistake" would merely mean that the actor held a belief (theory) that was false.

Randy Barnett's (District Attorney's Office, Cook County, IL) "Toward a Theory of Legal Naturalism" offered a sympathetic, but critical analysis of Lon L. Fuller's *Morality of Law*, a theory of legal process. He urged that natural law theorists integrate the insights of the Reformist Legal Realists into an organic theory of law.

Monday's sessions concluded with an ambitious paper by Frederic Jennings, Jr., (Economics, Stanford University). In "The Rand-Polanyi Synthesis and its Methodological Relevance to Economic Theory" he began with a critical summary of the debate on the methodology of Austrian economics. He then argued that this approach would benefit greatly from a reformulation based on a synthesis of Ayn Rand's theory of concepts and Michael Polanyi's emphasis on the personal element in concept formation. Jennings saw the approach as empirical in nature.

The first paper on Tuesday was Craig Bolton's (Economics; Denison University) "Methodological Individualism: An Appreciation and Clarification." Bolton explored the meaning and implications of methodological individualism, a key concept in Austrian economics. He sought to "indicate the proper scope and limits of methodological individualism, the different implications attendant upon its various interpretations, and the ties, if any, between methodological individualism and public policy questions." He contrasted Mises' Kantian epistemology, Rothbard's Thomist-Aristotelian views and the ideas of Karl Popper.

Gary Short (Economics; University of Virginia) provided a survey of the theories and problems of the "growth of knowledge" literature as they relate to the social sciences, and in particular to economics. The emphasis was on examining *Method and Appraisal in Economics* (edited by Spiro J. Latsis), a volume of essays which considered the application of Lakatos's Methodology of Scientific Research Programmes (MSRP) to economics. Short concluded that the growth of knowledge theories do not provide valid proscriptive statements about the social sciences since they were developed from the natural sciences and are not applicable to the different nature of the subject matter in the social world. As descriptive theories, however, they recognize the role of values in the evolution of science and are thus important for the social sciences.

"Incommensurability and Demarcation," a paper by John T. Sanders (Philosophy; Rochester Institute of Technology) was the subject of the last discussion on Tuesday. Sanders focused on Thomas Kuhn's thesis that scientific theories are incommensurable. He began with an examination of Kuhn's

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## The NYU Conference— Austrian Perspectives on Contemporary Economic Theory (Continued)

and offered the x-efficiency paradigm as an alternative framework where, contrary to the accepted approach, it is not assumed that all behavior is maximizing behavior.

Commenting on the Leibenstein paper, Professor Kirzner agreed that the entrepreneur does not fit within the world of general equilibrium since the entre-



Professor Harold Demsetz

preneur is driven by the desire for pure profits which exist only in disequilibrium. Kirzner stressed the importance of the entrepreneur as the driving force behind the economy and noted that this is a much stronger role than Liebenstein assigns the entrepreneur within his x-efficiency model. He was also critical of Liebenstein's contention that some of firm behavior does not fit the maximization hypothesis. Kirzner, citing Stigler's critique of x-efficiency, argued that non-profit maximizing behavior is not inefficient, but merely behavior aimed at goals other than monetary profit.

Following Kirzner's comments, Professor Harold Demsetz of UCLA presented his paper, "Ethics and Efficiency in Property Rights Systems." In this paper Demsetz argued that our notions of ethics and efficiency are closely related. His ideas are closely allied with the recent work on the relationship between economics and biology which attempts to relate the survival properties of efficient behavior to ethical views. Demsetz also took some libertarians to task for their insistence on treating property rights as sacrosanct rather than relative to efficiency criteria. In the course of his discussion, Demsetz demonstrated that Walter Block's criticisms of his work with Ronald Coase on private property rights depended on the

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## Austrian Economics Seminar, Part I: 1975-76 (Continued)

necessarily lead to economic inefficiency in terms of satisfying consumer welfare." The discussion surrounded the question of how analogous the subsidized lengthening of the structure of production in the "knowledge industry" is to normal Hayekian cycle theory: would such malinvestments be unsustainable, to what extent would specific capital be stuck in abandoned projects, and more fundamentally, can we speak of an optimal structure in the production of knowledge (as Lachmann noted, "Knowledge not yet had is unknowable before its time")?

It was argued that government subsidy of R and D would distort the market signals which suggest how much to invest in R and D and at what appropriate level of abstraction. Coordination requires that the individual entrepreneur spot the gaps in his own knowledge and select fruitful avenues for research investigation. Through government subsidy such decisions are taken out of the entrepreneur's hands and this is likely to lead to research which is unconnected to the production process.

While some of the fundamental internal controversies inherent in the various Austrian wings had come to the fore in minor skirmishes, it was with the fourth session (March 9th) that these issues were directly addressed. Lawrence White, then an undergraduate in economics at Harvard, presented a challenging paper entitled "Entrepreneurship, Imagination, and the Question of Equilibrium." Here the "nihilism" vs. "Ricardianism" issues emerged in the context of an inquiry into the nature of equilibrating forces. The Misesian approach performs a *ceteris paribus* mental experiment to observe the entrepreneur's coordinating role in pushing the market toward equilibrium. Yet this process of reaching an equilibrium, Lachmann argued, must itself change the distribution of resources, a datum supposedly frozen. It was not clear that "other things being equal" was meant to exclude the very consequences of the entrepreneur's actions. But, it was argued, the changes emanating from the actions of entrepreneurs move the equilibrium point towards which the coordination is headed. This coordination activity never comes to rest in the real world; however, White was asking whether it would come to rest *even if there were no other changes*.

As with many issues, apparent disagreement proved on further discussion to be more matters of terminology than

of substance. In Mises' approach there is one force operating, the entrepreneur's coordinating actions, which are described as equilibrating. Lachmann speaks of two forces, equilibrating and disequilibrating. The allegedly "nihilistic" tendency seems to derive, at least in part, from this apparently unpredictable balance between equilibrating and disequilibrating forces. Only where the former is "stronger" do we tend toward equilibrium. The charge of mechanistic Ricardianism is leveled against the Misesian approach for only concentrating on one of these forces and leading one to suppose we must usually be in equilibrium. But for the Misesian, Lachmann's disequilibrating forces are described as *movements* of the unattainable equilibrium toward which the equilibrating actions tend. Thus each approach deals with both kinds of forces, though in different ways. This is not to say that there is complete agreement underlying these terminological differences or that the approaches are equally fruitful in comprehending the market process.

A difference in emphasis emerged in the discussion concerning the description of entrepreneurship. In Kirzner's classic presentation of market process (*Competition and Entrepreneurship*) he concentrated on the arbitrage aspect of the entrepreneurial function and referred to spotting gaps in the market almost as if they were objectively present. Lachmann (and Mises) have always emphasized the futurity inherent in all action, and it does sometimes get awkward, as White pointed out, to discuss the spotting of an opportunity that does not yet exist. But Kirzner agreed that he had abstracted from the problems of time in that book and had intended to later extend his analysis to these problems (as he has done recently). While admitting some difficulty in speaking of the grasping of a future profit opportunity, it is nonetheless useful to see the arbitrage element in all entrepreneurship, just as it is useful to point out that all real world action is forward-looking into an uncertain future.

On April 6, 1976, the fifth session of the AES was honored to have Dr. Robert Nozick of Harvard present his extensive paper "On Austrian Methodology". This paper proved to be a rather ambitious task for a two hour discussion that ranged from methodological individualism to Darwinian evolution to time preference. Particularly interesting was

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policy measures. Rather, they are a manifestation of and a response to stock disequilibrium in the "money market" which will disappear when the disequilibrium has been adjusted. In other words, deficits and surpluses are merely transitory concomitants of a stock adjustment process.

Secondly, the automatic nature of the

stock equilibrium in the money market. Thus, the tools fashioned to alleviate payments disequilibria, e.g., export subsidies, import restrictions, exchange controls, devaluation, etc., can be dispensed with. The more radically consistent exponents of the monetary approach have also found Milton Fried-

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