

Study Guide to *Human Action* by Robert P. Murphy

Chapter XXVII. The Government and the Market

Chapter Summary

1. The Idea of a Third System

The systems of market economy and of socialism are neatly distinguished by whether the means of production are privately owned or owned by the government. If the government owns some enterprises but is able to calculate because other companies and capital goods are traded by private citizens, then this is not a "mixed economy" but rather a market economy where some property is owned by the government. Even so, many thinkers desire a system that is neither pure socialism nor pure capitalism—a system that allegedly avoids the evils in both extremes. Economics can inform us whether such a postulated third system can actually work in the fashion its proponents believe.

2. The Intervention

There are two patterns for the realization of socialism. Under the Lenin or Russian pattern, all enterprises are formally nationalized and become bureaucratic extensions of the state. In contrast, under the Hindenburg or German pattern, the appearance of a market is retained; there are nominal shopkeepers who pay wages and earn revenues, but these numbers are a sham, as all activity is directed by the central authority.

The two patterns are both cases of socialism. The German pattern is not characterized by interventionism, because the government has abolished the market. Under the interventionist approach, the government truly retains the institution of private property, but selectively interferes with outcomes it deems undesirable, using the threat of coercion to alter the actions that would have occurred on an unhampered market.

3. The Delimitation of Governmental Functions

Justice and morality only make sense in the context of society. It is useless to attempt to deduce the "legitimate" functions of government from an analysis of its nature. The purpose of government is to ensure the smooth operation of the market economy by enforcing respect for property rights. Governments obviously have the physical ability to intervene with wage and interest rates in their jurisdictions; the question is whether these measures will achieve their stated objectives.

4. Righteousness as the Ultimate Standard of the Individual's Actions

Some reformers suggest yet another possible social arrangement, where individuals voluntarily renounce greed and profits in order to satisfy ethical or religious ideals. Such a system, where people are led by conscience and not selfishness, would be neither socialism nor capitalism nor even interventionism (because the government would not enforce the new rules). However, it is not enough to tell entrepreneurs that they mustn't undersell their competitors, or that they must

pay reasonable wages to their employees. Once actors in a market are instructed to deviate from what they would have otherwise done, the reformers need to be specific in their guidelines.

5. The Meaning of Laissez Faire

In 18th-century France the classical liberals adopted the phrase *laissez faire, laissez passer* to describe their program. They wished to end government interference that crippled successful entrepreneurs from putting their inferior peers out of business. In modern times, "laissez-faire" has come to mean doing nothing in the face of unsatisfactory social conditions. The appeal of "planning" is precisely that it allegedly represents conscious action, as opposed to mindless and "automatic" market processes.

These popular conceptions are completely unfounded. The choice is not between planning or no planning; rather the choice is between allowing individuals the freedom to plan their own lives versus granting all power to the government. If a writer urges the government to overturn a market outcome, this really means that the writer wants armed men to implement the writer's own value system at the expense of the preferences of the consumers.

6. Direct Government Interference with Consumption

If the government directly interferes with the consumption choices of its subjects, catallactics has little to say. Economics deals with price determination by taking the willingness of consumers to spend as a given, without inquiring as to the motivations of this spending. However, in practice governments often attempt to mask their efforts by passing laws not directly on the masses but rather on the entrepreneurs who cater to them. Here is where economics can analyze whether such measures will achieve their stated goals.

Why It Matters

Now that Mises has explained the operation of a market economy, and has demonstrated the infeasibility of socialism, he turns to the suggested third way, namely, a mixed economy that allegedly escapes the evils of either extreme. In this modest chapter, Mises prepares the subject. In subsequent chapters, he will show that this alleged middle path is an unstable, untenable option. The choice still remains for people to choose either capitalism or socialism.

Technical Notes

- (1) Although Mises is quite hostile (pp. 716–717) to the idea of natural law—even as deployed by classical liberals whose economic views are quite similar to Mises's—Murray Rothbard and other Misesians were champions of this approach. Rothbard believes that reasoning on the nature of man and his environment can indeed provide guidance to jurists.
- (2) In his discussion of proposals for a moral social reform (pp. 719–725), Mises's harsh criticisms may mislead the reader. In an unhampered market economy, people make decisions not simply on the basis of "economic" considerations; people may donate to charities, and employers may retain employees at a monetary loss for nonpecuniary

reasons. All of these motivations contribute to the price structure of an unhampered market. But it is precisely this outcome that the reformers do not endorse. Mises's point, then, is that if people are told that their voluntary actions (guided perhaps by Christian teachings) are impermissible, then they must be given specific alternative criteria for their conduct.

- (3) In his discussion of direct government interference with consumption (pp. 727–729), Mises says that the prices of goods are dependent on consumer demand, and that the reason for this demand (i.e., whether legitimate consumer preference, or whether government compulsion) is irrelevant. But under many settings, this distinction would in fact lead to different outcomes. For example, the quality of the products would be different, depending on whether the consumers were purchasing them voluntarily, or were merely forced to by the government. However, Mises is trying to isolate the necessary praxeological flaws with interventionism, and therefore focuses his attention on interventionism's failure to achieve its own stated ends.

Study Questions

1. The Idea of a Third System

- What is the third way? What are its characteristics?

2. The Intervention

- What are the two patterns for the realization of socialism?
- What distinguishes interventionism from the German pattern of socialism?
- What does government interference always imply?

Comment: "The essential feature of government is the enforcement of its decrees by beating, killing, and imprisoning."

3. The Delimitation of Governmental Functions

Comment: "The notion of right and wrong is a human device, a utilitarian precept designed to make social cooperation under the division of labor possible."

- Does Mises think "Thou shalt not kill" is part of natural law?

4. Righteousness as the Ultimate Standard of the Individual's Actions

- Why would the market economy become a chaotic muddle if the predominance of private property—which the reformers disparage as selfishness—is eliminated?
- What is wrong with the desire for an "altruistic entrepreneur"?

- Why does Mises think the doctrine of just prices and wages would have arrested economic development?
- Why should the sermonizers appeal to consumers, rather than producers?

5. The Meaning of Laissez Faire

- What is the definition of laissez-faire?
- Does the market rely on "automatic" forces?

6. Direct Government Interference with Consumption

Comment: "Every act of government interference with business must indirectly affect consumption."

Comment: "If one abolishes man's freedom to determine his own consumption, one takes all freedoms away."