

**THE CLASH OF  
GROUP INTERESTS  
AND  
OTHER ESSAYS**

by

**Ludwig von Mises**

**Richard M. Ebeling, Editor  
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# Preface

by Murray N. Rothbard

In the twentieth century, the advocates of free market economics almost invariably pin the blame for government intervention solely on erroneous ideas—that is, on incorrect ideas about which policies will advance the public weal. To most of these writers, any such concept as “ruling class” sounds impossibly Marxist. In short, what they are really saying is that there are no irreconcilable conflicts of class or group interest in human history, that everyone’s interests are always compatible, and that therefore any political clashes can only stem from misapprehensions of this common interest.

In “The Clash of Group Interests,” the most important of the little-known essays reprinted here, Ludwig von Mises, the outstanding champion of the free market in this century, avoids the naive trap embraced by so many of his colleagues. Instead, Mises sets forth a highly sophisticated and libertarian theory of classes and of class conflict, by distinguishing sharply between the free market and government intervention. It is true that on the *free market* there are no clashes of class or group interest; all participants benefit from the market and therefore all their interests are in harmony. But the matter changes drastically, Mises points out, when we move to the intervention of government. For that very intervention necessarily *creates* conflict between those classes of people who are benefited or privileged by the State, and those who are burdened by it. These conflicting classes created by State intervention Mises calls *castes*. As Mises states:

Thus there prevails a solidarity of interests among all caste members and a conflict of interests among the various castes. Each privileged caste aims at the attainment of new privileges and at the preservation of old ones. Each underprivileged caste aims at the abolition of its disqualifications. Within a caste society there is an irreconcilable antagonism between the interests of the various castes.

In this profound analysis Mises harkens back to the original libertarian theory of class analysis, originated by Charles Comte and Charles Dunoyer, leaders of French *laissez-faire* liberalism in the early 19th century.

But Mises has a grave problem; as a utilitarian, indeed as someone who equates utilitarianism with economics and with the free market, he has to be able to convince *everyone*, even those whom he concedes are the ruling castes, that they would be better off in a free market and a free society, and that they too should agitate for this end. He attempts to do this by setting up a dichotomy between “short-run” and “long-run” interests, the latter being termed “the rightly understood” interests. Even the short-run beneficiaries from statism, Mises asserts, will lose in the long run. As Mises puts it:

In the short run an individual or a group may profit from violating the interests of other groups or individuals. But in the long run, in indulging in such actions, they damage their own selfish interests no less than those of the people they have injured. The sacrifice that a man or a group makes in renouncing some short-run gains, lest they endanger the peaceful operation of the apparatus of social cooperation, is merely temporary. It amounts to an abandonment of a small immediate profit for the sake of incomparably greater advantages in the long run.

The great problem here is: why *should* people always consult their long-run, as contrasted to their short-run, interests? Why is the long-run the “right understanding”? Ludwig von Mises, more than any economist of his day, has brought to the discipline the realization of the great and abiding importance of *time preference* in human action: the preference of achieving a given satisfaction now rather than later. In short, everyone prefers the shorter to the longer run, some to different degrees than others. How can Mises, as a utilitarian, say that a lower time preference for the present is “better” than a higher? In brief, some moral doctrine beyond utilitarianism is necessary to assert that people *should* consult their long-run over their short-run interests. This consideration becomes even more important when we consider those cases where government intervention confers great, not “small,” gains on the privileged, and where retribution does not arrive for a very long time, so that the “temporary” in the above quote is a long time indeed.

This consideration becomes still more poignant in the noble and surprising essay, “The Freedom to Move as an International Problem,” newly translated from a 1935 newspaper in Vienna. It is surprising because it presents a remarkably sharp attack on the immigration barriers erected by the United States and the British Dominions. For Mises trenchantly identifies these barriers as creating a ruling class elite, albeit a large one, in which workers in a particular geographical area with a high standard of living, use the State to keep immigrants from lower-wage areas out, thereby freezing the latter into a permanently lower wage. Mises correctly adds that, contrary to the Marxian myth of the

international solidarity of the proletariat, it is the unions in the high living standard countries who have lobbied for the immigration restrictions. Mises is hard-hitting on the privileges conferred by immigration barriers: "The oft-referred-to 'miracle' of the high wages in the United States and Australia may be explained simply by the policy of trying to prevent a new immigration. For decades people have not dared to discuss these things in Europe." Mises concludes his essay with an implicit justification of overcrowded Europe making war upon the restrictive countries: "This is a problem of the right of immigration into the largest and most productive lands. . . . Without the reestablishment of freedom of migration throughout the world, there can be no lasting peace."

Even here, Mises tries to show that, in the long run, the workers of the privileged countries are worse off from the immigration barriers, but it is clear that the "run" is so long and the intermediary advantages so substantial, that the utilitarian harmony of universal interests here breaks down.

The same breakdown occurs when Mises, in his "The Clash of Group Interests," tries to dismiss war between nations and nationalisms as senseless, at least in the long run. But he does not come to grips with the problem of national boundaries; since the essence of the nation-State is that it has a monopoly of force over a given territorial area, there is ineluctably a conflict of interest between States and their rulers over the size of their territories, the size of the areas over which their dominion is exercised. While in the free market, each man's gain is another man's gain, one State's gain in territory is necessarily another State's loss, and so the conflict of interest over boundaries are irreconcilable—even though they are less important the fewer the government interventions in society.

Mises' notable theory of classes has been curiously neglected by most of his followers. By bringing it back into prominence, we have to abandon the cozy view that all of us, we *and* our privileged rulers alike, are in a continuing harmony of interest. By amending Mises' theory to account for time preference and other problems in his "rightly understood" analysis, we conclude with the still less cozy view that the interests of the State privileged and of the rest of Society are at loggerheads. And further, that only moral principles beyond utilitarianism can ultimately settle the dispute between them.



# The Clash of Group Interests

## I

To apply the term “group tensions” to denote contemporary antagonisms is certainly a euphemism. What we have to face are conflicts considered as irreconcilable and resulting in almost continual wars, civil wars, and revolutions. As far as there is peace, the reason is not, to be sure, love of peace based on philosophical principles, but the fact that the groups concerned have not yet finished their preparations for the fight and, for considerations of expediency, are waiting for a more propitious moment to strike the first blow.

In fighting one another, people are not in disagreement with the consensus of contemporary social doctrines. It is an almost generally accepted dogma that there exist irreconcilable conflicts of group interests. Opinions differ by and large only with regard to the question, which groups have to be considered as genuine groups and, consequently, which conflicts are the genuine ones. The nationalists call the nations (which means in Europe the linguistic groups), the racists call the races, and the Marxians call the “social classes,” the genuine groups. but there is unanimity with regard to the doctrine that a genuine group cannot prosper except to the detriment of other genuine groups. The natural state of intergroup relations, according to this view, is conflict.

This social philosophy has made itself safe against any criticism by proclaiming the principle of polylogism. Marx, Dietzgen, and the radicals among the representatives of the “sociology of knowledge” teach that the logical structure of mind is different with different social classes. If a man deviates from the teachings of Marxism, the reason is either that he is a member of a nonproletarian class and therefore constitutionally

incapable of grasping the proletarian philosophy; or, if he is a proletarian, he is simply a traitor. Objections raised to Marxism are of no avail because their authors are "sycophants of the bourgeoisie." In a similar way the German racists declare that the logic of the various races is essentially different. The principles of "non-Aryan" logic and the scientific theories developed by its application are invalid for the "Aryans."

Now, if this is correct, the case for peaceful human cooperation is hopeless. If the members of the various groups are not even in a position to agree with regard to mathematical and physical theorems and biological problems, they will certainly never find a pattern for a smoothly functioning social organization.

It is true that most of our contemporaries, in their avowal of polylogism do not go so far as the consistent Marxians, racists, etc. But a vicious doctrine is not rendered less objectionable by timidity and moderation in its expression. It is a fact that contemporary social and political science makes ample use of polylogism, although its champions refrain from expounding clearly and openly the philosophical foundations of polylogism's teachings. Thus, for instance, the Ricardian theory of foreign trade is simply disposed of by pointing out that it was the "ideological superstructure" of the class interests of the nineteenth-century British bourgeoisie. Whoever opposes the fashionable doctrines of government interference with business or of labor-unionism is—in Marxian terminology—branded as a defender of the unfair class interests of the "exploiters."

The very way in which social scientists, historians, editors, and politicians apply the terms "capital" and "labor" or deal with the problems of economic nationalism is the proof that they have entirely adopted the doctrine of the irreconcilable conflict of group interests. If it is true that such irreconcilable conflicts exist, neither international war nor civil war can be avoided.

Our wars and civil wars are not contrary to the social doctrines generally accepted today. They are precisely the logical outcome of these doctrines.

## II

The first question we must answer is: What integrates those groups whose conflicts we are discussing?

Under a caste system the answer is obvious. Society is divided into rigid castes. Caste membership assigns to each individual certain privileges (*privilegia favorabilia*) or certain disqualifications (*privilegia odiosa*). As a rule a man inherits his caste quality from his parents, remains in his caste for life, and bestows his status on his children. His personal fate is inseparably linked with that of his caste. He cannot expect an improvement of his conditions except through an improve-



ment in the conditions of his caste or estate. Thus there prevails a solidarity of interests among all caste members and a conflict of interests among the various castes. Each privileged caste aims at the attainment of new privileges and at the preservation of the old ones. Each underprivileged caste aims at the abolition of its disqualifications. Within a caste society there is an irreconcilable antagonism between the interests of the various castes.

Capitalism has substituted equality under the law for the caste system of older days. In a free-market society, says the liberal economist, there are neither privileged nor underprivileged. There are no castes and therefore no caste conflicts. There prevails full harmony of the rightly understood (we say today, of the long-run) interests of all individuals and of all groups. The liberal economist does not contest the fact that a privilege granted to a definite group of people can further the short-term interests of this group at the expense of the rest of the nation. An import duty on wheat raises the price of wheat on the domestic market and thus increases the income of domestic farmers. (As this is not an essay on economic problems we do not need to point out the special-market situation required for this effect of the tariff.) But it is unlikely that the consumers, the great majority, will lastingly acquiesce in a state of affairs which harms them for the sole benefit of the wheat growers. They will either abolish the tariff or try to secure similar protection for themselves. If all groups enjoy privileges, only those are really benefited who are privileged to a far greater degree than the rest. With equal privilege for each group, what a man profits in his capacity as producer and seller is, on the other hand, absorbed by the higher prices he must pay in his capacity as consumer and buyer. But beyond this, all are losers because the tariff diverts production from the places offering the most favorable conditions for production to places offering less favorable conditions and thus reduces the total amount of the national income. The short-run interests of a group may be served by a privilege at the expense of other people. The rightly understood, *i.e.*, the long-run interests are certainly better served in the absence of any privilege.

The fact that people occupy the same position within the frame of a free-market society does not result in a solidarity of their short-run interests. On the contrary, precisely this sameness of their place in the system of the division of labor and social co-operation makes them competitors and rivals. The short-run conflict between competitors can be superseded by the solidarity of the rightly understood interests of all members of a capitalist society. But—in the absence of group privileges—it can never result in group solidarity and in an antagonism between the interests of the group and those of the rest of society. Under free trade the manufacturers of shoes are simply competitors. They can be

welded together into a group with solidarity of interests only when privilege supervenes, e.g., a tariff on shoes (*privilegium favorabile*) or a law discriminating against them for the benefit of some other people (*privilegium odiosum*).

It was against this doctrine that Karl Marx expounded his doctrine of the irreconcilable conflict of class interests. There are no castes under capitalism and bourgeois democracy. But there are social classes, the exploiters and the exploited. The proletarians have one common interest, the abolition of the wages system and the establishment of the classless society of socialism. The bourgeois, on the other hand, are united in their endeavors to preserve capitalism.

Marx's doctrine of class war is entirely founded on his analysis of the operation of the capitalist system and his appraisal of the socialist mode of production. His economic analysis of capitalism has long since been exploded as utterly fallacious. The only reason which Marx advanced in order to demonstrate that socialism is a better system than capitalism was his pretension to have discovered the law of historical evolution; namely, that socialism is bound to come with "the inexorability of a law of nature." As he was fully convinced that the course of history is a continuous progress from lower and less desirable modes of social production toward higher and more desirable modes and that therefore each later stage of social organization must necessarily be a better stage than the preceding stages were, he could not have any doubts about the blessings of socialism. Having quite arbitrarily taken for granted that the "wave of the future" is driving mankind toward socialism, he believed that he had done everything that was needed to prove the superiority of socialism. Marx not only refrained from any analysis of a socialist economy. He outlawed such studies as utterly "utopian" and "unscientific."

Every page of the history of the past hundred years belies the Marxian dogma that the proletarians are necessarily internationally minded and know that there is an unshakable solidarity of the interests of the wage-earners all over the world. Delegates of the "labor" parties of various countries have consorted with one another in the various International Working Men's Associations. But while they indulged in the idle talk about international comradeship and brotherhood, the pressure groups of labor of various countries were busy in fighting one another. The workers of the comparatively underpopulated countries protect, by means of immigration barriers, their higher standard of wages against the tendency toward an equalization of wage rates, inherent in a system of free mobility of labor from country to country. They try to safeguard the short-run success of "pro-labor" policies by barring commodities produced abroad from access to the domestic market of their own countries. Thus they create those tensions which must result in war

whenever those injured by such policies expect that they can brush away by violence the measures of foreign governments that are prejudicial to their own well-being.

Our age is full of serious conflicts of economic group interests. But these conflicts are not inherent in the operation of an unhampered capitalist economy. They are the necessary outcome of government policies interfering with the operation of the market. They are not conflicts of Marxian classes. They are brought about by the fact that mankind has gone back to group privileges and thereby to a new caste system.

In a capitalist society the proprietary class is formed of people who have well succeeded in serving the needs of the consumers and of the heirs of such people. However, past merit and success give them only a temporary and continually contested advantage over other people. They are not only continually competing with one another, they have daily to defend their eminent position against newcomers aiming at their elimination. The operation of the market steadily removes incapable capitalists and entrepreneurs and replaces them by parvenus. It again and again makes poor men rich and rich men poor. The characteristic features of the proprietary class are that the composition of its membership is continually changing, that entrance into it is open to everybody, that continuance in membership requires an uninterrupted sequence of successful business operations, and that the membership is divided against itself by competition. The successful businessman is not interested in a policy of sheltering the unable capitalists and entrepreneurs against the vicissitudes of the market. Only the incompetent capitalists and entrepreneurs (mostly later generations) have a selfish interest in such "stabilizing" measures. However, within a world of pure capitalism, committed to the principles of a consumers' policy, they have no chance to secure such privileges.

But ours is an age of producers' policy. Present day "unorthodox" doctrines consider it as the foremost task of a good government to place obstacles in the way of the successful innovator for the sole benefit of less efficient competitors and at the expense of the consumers. In the predominantly industrial countries the main feature of this policy is the protection of domestic farming against the competition of foreign agriculture working under more favorable physical conditions. In the predominantly agricultural countries it is, on the contrary, the protection of domestic manufacturing against the competition of foreign industries producing at lower costs. It is a return to the restrictive economic policies abandoned by the liberal countries in the course of the eighteenth and nineteenth centuries. If people had not discarded these policies then, the marvelous economic progress of the capitalist era would never have been achieved. If the European countries had not opened their frontiers to the importation of American products—cotton, tobac-

co, wheat, etc.—and if the older generations of Americans had rigidly barred the importation of European manufactures, the United States would never have reached its present stage of economic prosperity.

It is this co-called producers' policy that integrates groups of people, who otherwise would consider each other simply as competitors, into pressure groups with common interests. When the railroads came into being, the coach drivers could not consider joint action against this new competition. The climate of opinion would have rendered such a struggle futile. But today the butter producers are successfully struggling against margarine and the musicians against recorded music. Present-day international conflicts are of the same origin. The American farmers are intent upon barring access to Argentinian cereals, cattle, and meat. European countries are acting in the same way against the products of the Americans and of Australia.

The root causes of present-day group antagonisms must be seen in the fact that we are on the point of going back to a system of rigid castes. Australia and New Zealand are democratic countries. If we overlook the fact that their domestic policies are breeding domestic pressure groups fighting one another, we could say that they have built up homogeneous societies with equality under the law. But under their immigration laws, barring access not only to colored but no less to white immigrants, they have integrated their whole citizenry into a privileged caste. Their citizens are in a position to work under conditions safeguarding a higher productivity of the individual's work and thereby higher wages. The nonadmitted foreign workers and farmers are excluded from enjoyment of such opportunities. If an American labor union bars colored Americans from access to its industry, it converts the racial difference into a caste quality.

We do not have to discuss the problem whether or not it is true that the preservation and the further development of occidental civilization require the maintenance of the geographical segregation of various racial groups. The task of this paper is to deal with the economic aspects of group conflicts. If it is true that racial considerations make it inexpedient to provide an outlet for the colored inhabitants of comparatively overpopulated areas, this would not contradict the statement that in an unhampered capitalist society there are no irreconcilable conflicts of group interests. It would only demonstrate that racial factors make it inexpedient to carry the principle of capitalism and market economy in its utmost consequences and that the conflict among various races is, for reasons commonly called noneconomic, irreconcilable. It would certainly not disprove the statement of the liberals that within a society of free enterprise and free mobility of men, commodities, and capital, there are no irreconcilable conflicts of the rightly understood interests of various individuals and groups of individuals.

### III

The belief that there prevails an irreconcilable conflict of group interests is age-old. It was the essential proposition of Mercantilist doctrine. The Mercantilists were consistent enough to deduce from this principle that war is an inherent and eternal pattern of human relations. Mercantilism was a philosophy of war.

I want to quote two late manifestations of this doctrine. First a dictum of Voltaire. In the days of Voltaire the spell of Mercantilism had already been broken. French Physiocracy and British Political Economy were on the point of supplanting it. But Voltaire was not yet familiar with the new doctrines, although one of his friends, David Hume, was their foremost champion. Thus he wrote in 1764 in his *Dictionnaire Philosophique*: "*être bon patriote, c'est souhaiter que sa ville s'enrichisse par le commerce et soit puissante par les armes. Il est clair qu'un pays ne peut gagner sans qu'un autre perde, et qu'il ne peut vaincre sans faire des malheureux.*"\* Here we have in beautiful French the formula of modern warfare, both economic and military. More than eighty years later we find another dictum. Its French is less perfect, but its phrasing is more brutal. Says Prince Louis Napoleon Bonaparte, the later Emperor Napoleon III: "*La quantité des marchandises qu'un pays exporte est toujours en raison directe du nombre des boulets qu'il peut envoyer à ses ennemis, quand son honneur et sa dignité le commandent.*"\*\*

Against the background of such opinions we must hold the achievements of the classical economists and of the liberal policies inspired by them. For the first time in human history a social philosophy emerged that demonstrated the harmonious concord of the rightly understood interests of all men and of all groups of men. For the first time a philosophy of peaceful human co-operation came into being. It represented a radical overthrow of traditional moral standards. It was the establishment of a new ethical code.

All older schools of morality were heteronomous. They viewed the moral law as a restraint imposed upon man by the unfathomable decrees of Heaven or by the mysterious voice of conscience. Although a mighty group has the power to improve its own earthly well-being by inflicting damage upon weaker groups, it should abide by the moral law and forego furthering its own selfish interests at the expense of the

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\*["To be a good patriot is to hope that one's town enriches itself through commerce and is powerful in arms. It is clear that a country cannot gain unless another loses and it cannot prevail without making others miserable." —ed.]

\*\**Extinction du Pauperisme*, ed. Paris, 1848, p. 6. ["The quantity of goods which a country exports is always directly related to the number of bullets which it can send against its enemies with honor and dignity demanded"—ed.]

weak. The observance of the moral law amounts to sacrificing some advantage which the group or the individual could possibly secure.

In the light of the economic doctrine things are entirely different. There are, within an unhampered market society, no conflicts among the rightly understood selfish interests of various individuals and groups. In the short run an individual or a group may profit from violating the interests of other groups or individuals. But in the long run, in indulging in such actions, they damage their own selfish interests no less than those of the people they have injured. The sacrifice that a man or a group makes in renouncing some short-run gains, lest they endanger the peaceful operation of the apparatus of social co-operation, is merely temporary. It amounts to an abandonment of a small immediate profit for the sake of incomparably greater advantages in the long run.

Such is the core of the moral teachings of nineteenth-century utilitarianism. Observe the moral law for your own sake, neither out of fear of hell nor for the sake of other groups, but for your own benefit. Renounce economic nationalism and conquest, not for the sake of foreigners and aliens, but for the benefit of your own nation and state.

It was the partial victory of this philosophy that resulted in the marvelous economic and political achievements of modern capitalism. It is its merit that today there are living many more people on the earth's surface than at the eve of the "industrial revolution," and that in the countries most advanced on the way to capitalism the masses enjoy a more comfortable life than the well-to-do of earlier ages.

The scientific basis of this utilitarian ethics was the teachings of economics. Utilitarian ethics stands and falls with economics.

It would, of course, be a faulty mode of reasoning to assume beforehand that such a science of economics is possible and necessary because we approve of its application to the problem of peace preservation. The very existence of a regularity of economic phenomena and the possibility of a scientific and systematic study of economic laws must not be postulated *a priori*. The first task of any preoccupation with the problems commonly called economic is to raise the epistemological question whether or not there is such a thing as economics.

What we must realize is this: if this scrutiny of the epistemological foundations of economics were to confirm the statements of the German Historical School and of the American Institutionalists that there is no such thing as an economic theory and that the principles upon which the economists have built their system are illusory, then violent conflicts among various races, nations, and classes are inevitable. Then the militarist doctrine of perpetual war and bloodshed must be substituted for the doctrine of peaceful social co-operation. The advocates of peace are fools. Their program stems from ignorance of the basic problems of human relations.

There is no social doctrine other than that of the "orthodox" and "reactionary" economists that allows the conclusion that peace is desirable and possible. Of course, the Nazis promise us peace for the time after their final victory, when all other nations and races will have learned that their place in society is to serve as slaves of the Master Race. The Marxians promise us peace for the time after the final victory of the proletarians, precisely, in the words of Marx, after the working class will have passed "through long struggles, through a whole series of historical processes, wholly transforming both circumstances and men."\*

This is meager consolation indeed. At any rate, such statements do not invalidate the proposition that nationalists and Marxians consider the violent conflict of group interests as a necessary phenomenon of our time and that they attach a moral value either to international war or to class war.

#### IV

The most remarkable fact in the history of our age is the revolt against rationalism, economics, and utilitarian social philosophy; it is at the same time a revolt against freedom, democracy, and representative government. It is usual to distinguish within this movement a left wing and a right wing. The distinction is spurious. The proof is that it is impossible to classify in either of these groups the great leaders of the movement. Was Hegel a man of the Left or of the Right? Both the left wing and the right wing Hegelians were undoubtedly correct in referring to Hegel as their master. Was George Sorel a Leftist or a Rightist? Both Lenin and Mussolini were his intellectual disciples. Bismarck is commonly regarded as a reactionary. But his social-security scheme is the acme of present-day progressivism. If Ferdinand Lassalle had not been the son of Jewish parents, the Nazis would call him the first German labor leader and the founder of the German socialist party, one of their greatest men. From the point of view of true liberalism, all the supporters of the conflict doctrine form one homogenous party.

The main weapon applied by both the right and the left wing anti-liberals is calling their adversaries names. Rationalism is called superficial and unhistoric. Utilitarianism is branded as a mean system of stockjobber ethics. In the non-Anglo-Saxon countries it is, besides, qualified as a product of British "peddler mentality" and of American "dollar philosophy." Economics is scorned as "orthodox," "reactionary," "economic royalism" and "Wall Street ideology."

It is a sad fact that most of our contemporaries are not familiar with economics. All the great issues of present-day political controversies are

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\*Marx, *Der Buergerkrieg in Frankreich*, ed. by Pfemfert, Berlin, 1919, p. 54.

economic. Even if we were to leave out of account the fundamental problem of capitalism and socialism, we must realize that the topics daily discussed on the political scene can be understood only by means of economic reasoning. But people, even the civic leaders, politicians, and editors, shun any serious occupation with economic studies. They are proud of their ignorance. They are afraid that a familiarity with economics might interfere with the naive self-confidence and complacency with which they repeat slogans picked up by the way.

It is highly probable that not more than one out of a thousand voters knows what economists say about the effects of minimum wage rates, whether fixed by government decree or by labor-union pressure and compulsion. Most people take it for granted that to enforce minimum wage rates above the level of wage rates which would have been established on an unhampered labor market is a policy beneficial to all those eager to earn wages. They do not suspect that such minimum wage rates must result in permanent unemployment of a considerable part of the potential labor force. They do not know that even Marx flatly denied that labor unions can raise the income of all workers and that the consistent Marxians in earlier days therefore opposed any attempts to decree minimum wage rates. Neither do they realize that Lord Keynes's plan for the attainment of full employment, so enthusiastically endorsed by all "progressives," is essentially based on a reduction of the height of *real* wage rates. Keynes recommends a policy of credit expansion because he believes that "gradual and automatic lowering of real wages as a result of rising prices" would not be so strongly resisted by labor as any attempt to lower money wage rates.\* It is not too bold a statement to affirm that with regard to this primordial problem the "progressive" experts do not differ from those popularly disparaged as "reactionary labor baiters." But then the doctrine that there prevails an irreconcilable conflict of interests between employers and employees is deprived of any scientific foundation. A lasting rise in wage rates for all those eager to earn wages can be attained only by the accumulation of additional capital and by the improvement in technical methods of production which this additional wealth makes feasible. The rightly understood interests of employers and employees coincide.

It is no less probable that only small groups realize the fact that the free traders object to the various measures of economic nationalism because they consider such measures as detrimental to the welfare of their own nation, not because they are anxious to sacrifice the interests

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\*Keynes, *The General Theory of Employment, Interest and Money*, London, 1939, p. 264. For a critical examination of this idea see Albert Hahn, *Deficit Spending and Private Enterprise*. Postwar Readjustments Bulletin, No. 8, U.S. Chamber of Commerce, pp. 28-29.



of their fellow citizens to those of foreigners. It is beyond doubt that hardly any German, in the critical years preceding Hitler's rise to power, understood that those fighting aggressive nationalism and eager to prevent a new war were not traitors, ready to sell the vital interests of the German nation to foreign capitalism, but patriots who wanted to spare their fellow citizens the ordeal of a senseless slaughter.

The usual terminology classifying people as friends or foes of labor and as nationalists or internationalists, is indicative of the fact that this ignorance of the elementary teachings of economics is an almost universal phenomenon. The conflict philosophy is firmly entrenched in the minds of our contemporaries.

One of the objections raised against the liberal philosophy recommending a free-market society runs this way: "Mankind can never go back to any system of the past. Capitalism is done for because it was the social organization of the nineteenth century, an epoch that has passed away."

However, what these would-be progressives are supporting is tantamount to a return to the social organization of the ages preceding the "industrial revolution." The various measures of economic nationalism are a replica of the policies of Mercantilism. The jurisdictional conflicts between labor unions do not essentially differ from the struggles between mediaeval guilds and inns. Like the absolute princes of seventeenth- and eighteenth-century Europe, these moderns are aiming at a system under which the government undertakes the direction of all economic activities of its citizens. It is not consistent to exclude beforehand the return to the policies of Cobden and Bright if one does not find any fault in returning to the policies of Louis XIV and Colbert.

## V

It is a fact that the living philosophy of our age is a philosophy of irreconcilable conflict and dissociation. People value their party, class, linguistic group, or nation as supreme, believe that their own group cannot thrive but at the expense of other groups, and are not prepared to tolerate any measures which in their opinion would have to be considered as an abandonment of vital group interests. Thus a peaceful arrangement with other groups is out of the question. Take for instance the implacable intransigence of Leninism or of the French *nationalisme integral* or of the Nazis. It is the same with regard to domestic affairs. No pressure group is ready to renounce the least of its pretensions for considerations of national unity.

It is true that powerful forces are fortunately still counteracting these tendencies toward disintegration and conflict. In this country the traditional prestige of the Constitution is such a factor. It has nipped in the bud the endeavors of various local pressure groups to break up the

economic unity of the nation by the establishment of interstate trade barriers. But in the long run even these noble traditions may prove insufficient if not backed by a social philosophy, positively, proclaiming the primacy of the interests of the Great Society and their harmony with the rightly understood interests of each individual.\*

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\*[See, Ludwig von Mises', *Socialism, an Economic and Sociological Analysis* (London: Jonathan Cape, revised ed., 1951) pp. 328-351, and *Theory and History, an Interpretation of Social and Economic Evolution* (Yale University Press, 1957) pp. 112-146, for a further development of the ideas presented in "The Clash of Group Interests" —ed.]

# The Myth of the Failure of Capitalism

(Translated by Jane E. Sanders)\*

The nearly universal opinion expressed these days is that the economic crisis of recent years marks the end of capitalism. Capitalism allegedly has failed, has proven itself incapable of solving economic problems, and so mankind has no alternative, if it is to survive, then to make the transition to a planned economy, to socialism.

This is hardly a new idea. The socialists have always maintained that economic crises are the inevitable result of the capitalistic method of production and that there is no other means of eliminating economic crises than the transition to socialism. If these assertions are expressed more forcefully these days and evoke greater public response, it is not because the present crisis is greater or longer than its predecessors, but rather primarily because today public opinion is much more strongly influenced by socialist views than it was in previous decades.

## I

When there was no economic theory, the belief was that whoever had power and was determined to use it could accomplish anything. In the interest of their spiritual welfare and with a view toward their reward in Heaven, rulers were admonished by their priests to exercise moderation in their use of power. Also, it was not a question of what limits the inherent conditions of human life and production set for this power, but rather that they were considered boundless and omnipotent in the sphere of social affairs.

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\*[The translator wishes to gratefully acknowledge the comments and suggestions of Professor John T. Sanders, Rochester Institute of Technology, and Professor David R. Henderson, University of Rochester, in the preparation of the translation.]

The foundation of social sciences, the work of a large number of great intellects, of whom David Hume and Adam Smith are most outstanding, has destroyed this conception. One discovered that social power was a spiritual one and not (as was supposed) a material and, in the rough sense of the word, a real one. And there was the recognition of a necessary coherence within market phenomena which power is unable to destroy. There was also a realization that something was operative in social affairs that the powerful could not influence and to which they had to accommodate themselves, just as they had to adjust to the laws of nature. In the history of human thought and science there is no greater discovery.

If one proceeds from this recognition of the laws of the market, economic theory shows just what kind of situation arises from the interference of force and power in market processes. The isolated intervention cannot reach the end the authorities strive for in enacting it and must result in consequences which are undesirable from the standpoint of the authorities. Even from the point of view of the authorities themselves the intervention is pointless and harmful. Proceeding from this perception, if one wants to arrange market activity according to the conclusions of scientific thought—and we give thought to these matters not only because we are seeking knowledge for its own sake, but also because we want to arrange our actions such that we can reach the goals we aspire to—one then comes unavoidably to a rejection of such interventions as superfluous, unnecessary, and harmful, a notion which characterizes the liberal teaching. It is not that liberalism wants to carry standards of value over into science; it wants to take from science a compass for market actions. Liberalism uses the results of scientific research in order to construct society in such a way that it will be able to realize as effectively as possible the purposes it is intended to realize. The politico-economic parties do not differ on the end result for which they strive but on the means they should employ to achieve their common goal. The liberals are of the opinion that private property in the means of production is the only way to create wealth for everyone, because they consider socialism impractical and because they believe that the system of interventionism (which according to the view of its advocates is between capitalism and socialism) cannot achieve its proponents' goals.

The liberal view has found bitter opposition. But the opponents of liberalism have not been successful in undermining its basic theory nor the practical application of this theory. They have not sought to defend themselves against the crushing criticism which the liberals have leveled against their plans by logical refutation; instead they have used evasions. The socialists considered themselves removed from this criticism,

because Marxism has declared inquiry about the establishment and the efficacy of a socialist commonwealth heretical; they continued to cherish the socialist state of the future as heaven on earth, but refused to engage in a discussion of the details of their plan. The interventionists chose another path. They argued, on insufficient grounds, against the universal validity of economic theory. Not in a position to dispute economic theory logically, they could refer to nothing other than some "moral pathos," of which they spoke in the invitation to the founding meeting of the *Vereins für Sozialpolitik* [*Association for Social Policy*] in Eisenach. Against logic they set moralism, against theory emotional prejudice, against argument the reference to the will of the state.

*Economic theory predicted the effects of interventionism and state and municipal socialism exactly as they happened.* All the warnings were ignored. For fifty or sixty years the politics of European countries has been anticapitalist and antiliberal. More than forty years ago Sidney Webb (Lord Passfield) wrote: ". . . it can now fairly be claimed that the socialist philosophy of to-day is but the conscious and explicit assertion of principles of social organization which have been already in great part unconsciously adopted. The economic history of the century is an almost continuous record of the progress of Socialism."\* That was at the beginning of this development and it was in England where liberalism was able for the longest time to hold off the anticapitalistic economic policies. Since then interventionist policies have made great strides. In general the view today is that we live in an age in which the "hampered economy" reigns—as the forerunner of the blessed socialist collective consciousness to come.

Now, because indeed that which economic theory predicted has happened, because the fruits of the anticapitalistic economic policies have come to light, a cry is heard from all sides: this is the decline of capitalism, the capitalistic system has failed!

Liberalism cannot be deemed responsible for any of the institutions which give today's economic policies their character. It was against the nationalization and the bringing under municipal control of projects which now show themselves to be catastrophes for the public sector and a source of filthy corruption; it was against the denial of protection for those willing to work and against placing state power at the disposal of the trade unions, against unemployment compensation, which has made unemployment a permanent and universal phenomenon, against social insurance, which has made those insured into grumblers, mal-

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\*Cf. Webb, *Fabian Essays in Socialism*. . . Ed. by G. Bernard Shaw. (American ed., edited by H.G. Wilshire. New York: The Humboldt Publishing Co., 1891) p. 4.

ingers, and neurasthenics, against tariffs (and thereby implicitly against cartels), against the limitation of freedom to live, to travel, or study where one likes, against excessive taxation and against inflation, against armaments, against colonial acquisitions, against the oppression of minorities, against imperialism and against war. It put up stubborn resistance against the politics of capital consumption. And liberalism did not create the armed party troops who are just waiting for the convenient opportunity to start a civil war.

## II

The line of argument that leads to blaming capitalism for at least some of these things is based on the notion that entrepreneurs and capitalists are no longer liberal but interventionist and statist. The fact is correct, but the conclusions people want to draw from it are wrong-headed. These deductions stem from the entirely untenable Marxist view that entrepreneurs and capitalists protected their special class interests through liberalism during the time when capitalism flourished but now, in the late and declining period of capitalism, protect them through interventionism. This is supposed to be proof that the "hampered economy" of interventionism is the historically necessary economics of the phase of capitalism in which we find ourselves today. But the concept of classical political economy and of liberalism as the ideology (in the Marxist sense of the word) of the bourgeoisie is one of the many distorted techniques of Marxism. If entrepreneurs and capitalists were liberal thinkers around 1800 in England and interventionist, statist, and socialist thinkers around 1930 in Germany, the reason is that entrepreneurs and capitalists were also captivated by the prevailing ideas of the times. In 1800 no less than in 1930 entrepreneurs had special interests which were protected by interventionism and hurt by liberalism.

Today the great entrepreneurs are often cited as "economic leaders." Capitalistic society knows no "economic leaders." Therein lies the characteristic difference between socialist economies on the one hand and capitalist economies on the other hand: in the latter, the entrepreneurs and the owners of the means of production follow no leadership save that of the market. The custom of citing initiators of great enterprises as economic leaders already gives some indication that these days it is not usually the case that one reaches these positions by economic successes but rather by other means.

In the interventionist state it is no longer of crucial importance for the success of an enterprise that operations be run in such a way that the needs of the consumer are satisfied in the best and least expensive way; it is much more important that one has "good relations" with the

controlling political factions, that the interventions redound to the advantage and not the disadvantage of the enterprise. A few more Marks worth of tariff-protection for the output of the enterprise, a few Marks less tariff-protection for the inputs in the manufacturing process can help the enterprise more than the greatest prudence in the conduct of operations. An enterprise may be well run, but it will go under if it does not know how to protect its interests in the arrangement of tariff rates, in the wage negotiations before arbitration boards, and in governing bodies of cartels. It is much more important to have "connections" than to produce well and cheaply. Consequently the men who reach the top of such enterprises are not those who know how to organize operations and give production a direction which the market situation demands, but rather men who are in good standing both "above" and "below," men who know how to get along with the press and with all political parties, especially with the radicals, such that their dealings cause no offense. This is that class of general directors who deal more with federal dignitaries and party leaders than with those from whom they buy or to whom they sell.

Because many ventures depend on political favors, those who undertake such ventures must repay the politicians with favors. There has been no big venture in recent years which has not had to expend considerable sums for transactions which from the outset were clearly unprofitable but which, despite expected losses, had to be concluded for political reasons. This is not to mention contributions to non-business concerns—election funds, public welfare institutions and the like.

Powers working toward the independence of the directors of the large banks, industrial concerns, and joint-stock companies from the stockholders are asserting themselves more strongly. This politically expedited "tendency for big businesses to socialize themselves," that is, for letting interests other than the regard "for the highest possible yield for the stockholders" determine the management of the ventures, has been greeted by statist writers as a sign that we have already vanquished capitalism.\* In the course of the reform of German stock rights, even legal efforts have already been made to put the interest and well-being of the entrepreneur, namely "his economic, legal, and social self-worth and lasting value and his independence from the changing majority of changing stockholders,"\*\* above those of the shareholder.

With the influence of the state behind them and supported by a thoroughly interventionist public opinion, the leaders of big enterprises

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\*Cf. Keynes, "The End of Laisser-faire," 1926, see, *Essays in Persuasion* (New York: W.W. Norton & Co., Inc., 1932) pp. 314-315.

\*\*Cf. Passow, *Der Strukturwandel der Aktiengesellschaft im Lichte der Wirtschaftsenquete*, (Jena 1939), S.4.

today feel so strong in relation to the stockholders that they believe they need not take their interests into account. In their conduct of the businesses of society in those countries in which statism has most strongly come to rule—for example in the successor states of the old Austro-Hungarian Empire—they are as unconcerned about profitability as the directors of public utilities. The result is ruin. The theory which has been advanced says that these ventures are too large to be run simply with a view toward profit. This concept is extraordinarily opportune whenever the result of conducting business while fundamentally renouncing profitability is the bankruptcy of the enterprise. It is opportune, because at this moment the same theory demands the intervention of the state for support of enterprises which are too big to be allowed to fail.

### III

It is true that socialism and interventionism have not yet succeeded in completely eliminating capitalism. If they had, we Europeans, after centuries of prosperity, would rediscover the meaning of hunger on a massive scale. Capitalism is still prominent enough that new industries are coming into existence, and those already established are improving and expanding their equipment and operations. All the economic advances which have been and will be made stem from the persistent remnant of capitalism in our society. But capitalism is always harassed by the intervention of the government and must pay as taxes a considerable part of its profits in order to defray the inferior productivity of public enterprise.

The crisis under which the world is presently suffering is the crisis of interventionism and of state and municipal socialism, in short the crisis of anticapitalist policies. Capitalist society is guided by the play of the market mechanism. On that issue there is no difference of opinion. The market prices bring supply and demand into congruence and determine the direction and extent of production. It is from the market that the capitalist economy receives its sense. If the function of the market as regulator of production is always thwarted by economic policies in so far as the latter try to determine prices, wages, and interest rates instead of letting the market determine them, then a crisis will surely develop.

*Bastiat has not failed, but rather Marx and Schmoller.*



## The Freedom To Move as an International Problem

(Translated by Bettina Bien Greaves)

Discussions of the problems of peace and of the League of Nations have made substantial progress in recent months. Today one very often hears that peace cannot be secured simply by decree. Rather, to create a lasting peace, conditions must first be established which make life without war possible. Since it is believed that the "unequal distribution of raw materials" is the primary source of the conflicts that could lead to war, the first thought is for a "more equitable" distribution of raw materials. However, it is not very clear just what this means.

Wool is produced primarily in Australia, cotton in the United States, India and Egypt. Is it now proposed to hand over a part of these territories to the European states who possess no wool or cotton producing areas of their own? Let us assume the most preposterous case, that the wool producing territories of Australia were parcelled out among the European states. How would this improve the situation of these European countries? After the new partition, the Europeans would still have to purchase wool, as they did before, from the producers of wool whose lives, after all, are no bed of roses today.

The English also buy wool in Australia. They too must pay for this wool, just as must every other buyer. The fact that the British king is also sovereign over Australia plays no role in these purchases. Australia is completely independent of England, the English Parliament and the English government—in its constitution, legislation, administration and all its political affairs. English industry is not benefitted, as com-

pared with its continental competition, because a considerable part of the raw materials it fabricates comes from the British Empire. It obtains raw materials in the same way and it pays as much as do German, Italian or Austrian manufacturers. The freight situation for British industry is usually more favorable but this fact would not be altered in anyway by a change of sovereignty. Thus, no one in Europe can say: I am suffering because the state to which I belong does not also include areas that are better suited for the production of raw materials. What Europeans complain about is something else.

There are extensive tracts of land, comparable to those in Europe, which are sparsely settled. The United States of America and the British dominions of Canada, Australia, New Zealand, South Africa and so on, are less heavily populated, in comparison with their nature-endowed potential for production, than are the lands of Europe. As a result, the productivity of labor is higher there than in Europe. Consequently also higher wages are paid there for labor.

Because those lands offer more favorable opportunities for production than Europe does, they have been the goals of would-be European emigrants for more than 300 years. However, the descendants of those earlier emigrants now say: There has been enough migration. We do not want other Europeans to do what our forefathers did when they emigrated to improve their situation. We do not want our wages reduced by a new contingent of workers from the homeland of our fathers. We do not want the migration of workers to continue until it brings about the equalization of the height of wages. Kindly stay in your old homeland, you Europeans, and be satisfied with lower wages.

The oft-referred to "miracle" of the high wages in the United States and Australia may be explained simply by the policy of trying to prevent a new immigration. For decades people have not dared to discuss these things in Europe. Public opinion has been led astray by the smoke-screen laid down by Marxist ideology which would have people believe that the union-organized "proletariat of all lands" have the same interests and that only entrepreneurs and capitalists are nationalistic. The hard fact of the matter—namely that the unions in all those countries which have more favorable conditions of production, relatively fewer workers and thus higher wages, seek to prevent an influx of workers from less favored lands—has been passed over in silence. At the same time that the labor unions in the United States of America and the British dominions were constructing immigration laws which prohibited practically all reinforcements, the Marxist pedants were writing their books claiming that the cause of imperialism and war was due to the drive of capitalists for profits and that the proletariat, united in harmony and a solidarity of interests, wanted peace.

No Italian should say that his interests are prejudiced by the fact

that the lands from which metals and textile raw materials are extracted do not look to the King of Italy as their ruler. Yet every Italian worker *does* suffer because these areas do not allow the immigration of Italian workers. For this barrier cancels out, or at least weakens, the evening out of the height of wages that accompanies the freedom to move. And the situation that prevails for Italian workers is equally valid also for Germans, Czechs, Hungarians and many others.

One must certainly be careful to avoid accepting the false interpretation that workers in lands where the natural conditions are more favorable for production can fare better by prohibiting immigration than they can if migration were free. If the European workers are prevented from emigrating and thus have to stay at home, this does not mean they will remain idle as a result. They will continue to work in their old homeland under less favorable conditions. And because of the less advantageous conditions of production there, they will be compensated in lower wages. They will then compete on the world market, as well as on the home market of the industry producing under more favorable conditions. These countries may then very likely strike out with tariffs and import embargoes against what they call the "unfair" competition of cheap labor. By doing this, they will be forfeiting the advantages which the higher division of labor brings. They will suffer because production opportunities which are more favorable, i.e. which bring a higher return with the same expenditure than do the production opportunities which must be used in other lands, are not being used in their own countries. If only the most productive resources were exploited everywhere over the earth's surface, and the less productive resources were left unused, their position would be better in the long run too. For then the total yield of the world's production would be greater. And out of this greater overall "pie," a larger portion would come to them.

The attempt to create certain industries artificially in the lands of eastern Europe, under the protection of tariffs and import embargoes, can certainly be considered a failure. Still, if the freedom of migration is not reestablished, the lower wages in those lands will attract capital and entrepreneurial effort. Then, in place of the hot-house industries, artificially fostered by governmental measures and unviable still in spite of these measures, industries with lower wages and lower living standards for the masses will develop there, industries which *will* be viable in view of the location. These people will certainly still have just as much cause to complain as before—not over the unequal distribution of raw materials, but over the erection of migration barriers around the lands with more favorable conditions of production. And it may be that one day they will reach the conclusion that only weapons can change this unsatisfactory situation. Thus, we may face a great coalition of the lands of would-be emigrants standing in opposition to the lands that

erect barricades to shut out would-be immigrants.

Through its affiliated office for intellectual cooperation the League of Nations is undertaking investigations as to how changes that call for general appeasement may be brought about without war. If these investigations and the conference, at which they will be presented, are concerned only with the problem of raw materials, then their efforts will have been in vain. The major problem will be side-stepped, also, if the proposals are merely for a new apportionment of the African colonies and mandated territories in Asia and Polynesia. The primary difficulties wouldn't be settled either, even if the German Reich were to receive back her old colonies enlarged, even if Italy's share of the African territory were expanded and even if the Czechs and the Hungarians were not forgotten.

What the European emigrants seek is land where Europeans can work under climatic conditions that are tolerable for them and where they can earn more than they can in their homeland, which is overpopulated and less well provided for by nature. Under present circumstances this can be offered only in the New World, in America and Australia. This is not a problem of raw materials. It is not a question as to which state should be given sovereignty over some colonies that are scarcely habitable by European emigrants. This is a problem of the right of immigration into the largest and most productive lands, the climates of which are suitable for white European workers. Without the reestablishment of freedom of migration throughout the world, there can be no lasting peace.

# Karl Menger and the Austrian School of Economics

(Translated by Albert Zlabinger)

On the day of the dedication of the memorial to Karl Menger in the arcade of the University of Vienna, it is only fitting to take a look at the work which the Austrian School of Economics, founded by Karl Menger, has produced. It is not a eulogy to dead and past things. Even if the men who have produced it have passed away, their work continues to live and has become the basis for all scientific endeavors in economic theory. No economic thinking can occur today without building on the basis of what Menger and his school have taught. It is generally accepted that the beginning of a new era in the history of our science is marked by the first scientific appearance of Menger on the scene with his *Grundsätze der Volkswirtschaftslehre* [*Principles of Economics*] published in 1871.

No other place is better suited for an attempt to provide a short overview for the general audience on the works of the Austrian School of economics than in the columns of the *Neue Freie Presse*. This is because Karl Menger himself and all the others who can be counted among the older Austrian school in the narrower or broader sense (Eugen v. Böhm-Bawerk, Friedrich Wieser, Robert Zuckerkandl, Emil Sax, Robert Meyer, Johann Komorzynski, Rudolf Auspitz, Richard Lieben), have spoken out again and again in the *Neue Freie Presse* in order to discuss economic issues of the day or to report about the results of the theoretical research.

## I

The historical starting point of scientific economics is the idea suggested by the Physiocrats in France and the Scotsmen David Hume and Adam Smith, that prices, wages, and interest rates are clearly determined by the market situation or at least within certain limits and that the market price functions as the regulator of production. Where earlier men saw only randomness and arbitrariness, they recognized a process of regularity. The classical school of economics whose contributions culminated in the work of David Ricardo, made it its task to develop catallactics, the science of exchange and income, into a complete system.

Based on the insights of the theoretical research, important conclusions for economic policy could be drawn. Gradually it was understood, that the interventions with which governments wanted to lead economic forces in a certain direction had to miss the target that was set. The setting of a maximum price cannot achieve the goal of providing the population with the cheapest supply; if the authoritarian order is carried out, this leads to the restriction if not the complete cessation of market supply of the goods in question. The intervention thus achieves the opposite of what was aimed at. This is similar to the authoritarian regulation of wages, interest rates and intervention in foreign trade. The Mercantilists believed that balance in foreign trade had to be secured through trade policies (tariffs, prohibitions, etc.) in order to prevent the outflow of money. Ricardo showed that this balance will be established automatically. Restrictions on foreign trade for the purpose of protecting the currency are superfluous as long as it is not being destroyed by inflation. On the other hand, these measures would be incapable of stopping the erosion of the purchasing power of the currency that is caused by inflation. Protective trade policies divert production from where it can best take advantage of natural conditions, and thus reduce the abundance produced by economic activity and depress the standard of living of the masses.

In the eyes of classical economists, the use of interventionism appears as counter-productive in every respect; it is not from the interventions by the government, which only can hinder and hamper, but from the free rein of all forces that they expect a continuing increase in the welfare of all groups. In this way, the political program of liberalism is based on the foundations of the teachings of the classical economists and requires unimpeded trade for domestic as well as international economic policy.

Those who wanted to attack liberalism had to attempt to disprove these conclusions. But this was an impossibility. The part of the teaching of the classical economists on which these conclusions rested was unshakeable. For the opponents of liberalism there was only one way out: they had to reject in principle, as the German historical school did, every science of the social economy that claimed general validity of its principles. Only economic history and descriptive economics was to be valid. Investigations of the fundamentals of the relationships of economic phenomena were declared "abstract" and "unscientific."

After Walter Bagehot, whose reputation as an economist is based on the famous book about the London money market, *Lombard Street*, had attacked these fallacies in the mid-70's, Menger appeared on the scene in 1883 with his book *Untersuchungun über die Methode der Sozialwissenschaften* [*Problems of Economics and Sociology*]. The discussions known as the "Methodenstreit" which followed this book have

successfully destroyed the logical and methodological validity of the criticism of the historical school against the fundamental possibility of generally valid insights into economic problems. Every economic inquiry of a historical or descriptive nature contains at least implicitly theoretical concepts and principles whose general validity has to be asserted. Without resorting to these, it is impossible to say anything. In every statement about the price of a good, attacks on a socio-political measure or a group interest must already contain "theory." The fact that the "Socialists of the Chair" have not noticed this, does not make them "free of theory." All they have done is to do without thorough investigation of the correctness of the theories that they have used, to follow them to their logical conclusion, to tie them together into a system and by doing so check them for contradictions and to show logical consistency and most of all to verify them against the facts. They have only replaced useful theories which can stand up against criticism with untenable contradictory and long disproven fallacies which they made the starting point of their inquiries which as a result have very little value.

The practice of economic theory entails constant sharp criticism of all statements of an economic nature with all means at the disposal of the human mind.

## II

The system of classical economics was unable to provide a satisfactory solution to the problem of price determination. It should have been obvious to derive the evaluation of goods which represents the basis of the price determination process, from their usefulness (usefulness in satisfying human wants). But there was a special difficulty, which the classical economists with all their ingenuity could not overcome. Some of the most useful goods are assigned a low value such as iron, coal or bread or are given no value at all such as water or air, whereas doubtless less useful ones such as gems are valued very highly. In view of the failure of all efforts to explain this paradox, it was decided to look for other explanations of value which however could not be thought out without artificial aids and without contradiction. Something was obviously wrong.

Menger succeeded in his ingenious first work to overcome this seeming paradox of value. It is not the importance of an entire category of goods that determines value, but the importance which is assigned to that part that is presently available. It is the value of the concrete partial quantity that influences price determination, not the value of the goods category. Since we assign each individual part of a given supply only the importance that is derived from the satisfaction of wants that it provides, and since in each individual category of wants the urgency of further satisfaction is reduced as satiation progresses, each concrete

partial quantity is valued on the basis of the importance of the last and least important of the concrete wants that can just be satisfied with the available supply (marginal utility). The price determination of goods of the first order, that is goods that serve the immediate use and consumption, is thus traced to the subjective evaluations of consumers. The prices of goods of higher order (also called means of production) which are necessary for the production of consumer goods, including the wage, i.e. the price for labor, are derived from the prices of goods of the first order. It is ultimately the consumers who determine and pay the prices of the means of production as well as the wages. To carry out this derivation in a specific case is the task of the theory of imputation which deals with the prices of land, wages, capital rent, and profit.

On these new foundations Menger and his followers built, by using principles established by the classical economists, a complete system for the explanation of economic phenomena.

### III

At about the same time and independently of Menger, the British economist William Stanley Jevons and the Frenchman Leon Walras, working in Lausanne, taught similar theories. After the time had passed which each new idea needs to prove itself, the subjective marginal utility theory began its victorious march through the world. Menger was more fortunate than his most significant forerunner, the Prussian government employee Gossen, and could witness the recognition of his teachings by economists throughout the world.

In the United States it was mainly John Bates Clark, the founder of the great American school, who applied the ideas of the Austrian school and expanded them. Clark is also—as Henry Oswald in Frankfurt and Richard Reisch—an honorary member of the Viennese Society for Economists. In the Netherlands and the Scandinavian countries, the teachings bore fruit early. But especially in Italy soon a successful scientific endeavor flourished on its basis.

Menger never formed a school of thought in the ordinary sense. He was too great and thought too much of the dignity of science to use the petty means which others availed themselves of to further their cause. He did research, wrote and taught and the best people who have worked for Austria's government and economy in the past decades have emerged from his school. Moreover, he waited, full of the optimism of the liberal, that reason will prevail eventually. And one day, two companions joined him who would continue his work. They were a decade younger than Menger and, as mature men, had worked their way to the problems with the help of Menger's writing. Eugen von Böhm-Bawerk and Friedrich von Wieser, of equal age and friends since their youth, related through marriage and bound together by conviction, character,



and culture of the spirit, were as different in their scientific personalities as only two contemporaries could be. Each in their own way started to continue the work where Menger left off. In the history of our science, their names cannot be separated from that of Menger.

Both of them have since brought their work and their lives to a close. However a new generation has moved up and the series of excellent scientific inquiries which have been published in the past few years by men under thirty shows that Austria is not willing to relinquish its position as the home of rigorous economic research.

#### IV

Originally, the historical school of the "Economic Science of the State" (*wirtschaftliche Staatswissenschaften*) was bothered very little by the critical and positive work of the Austrian school and in this respect was very similar to the schools of interventionism abroad. They continued to look down upon serious theoretical work and to spread without inhibition the teachings of the omnipotence of the State over the economy in the knowledge that their position of power was guaranteed by governments and political parties.

The experiments in economic policy which were carried out during the war and the years immediately following the war, catapulted interventionism and statism to the top. All these experiments, such as maximum prices, command economy, and inflation had the result that was predicted by the theoreticians that were so detested by statesmen and the representatives of the historical school. The opponents of the "abstract and unrealistic Austrian value theory" attempted to hold their position with obstinacy for a while. How far they went in their delusion is shown by the example of one of their members who was celebrated as an authority on monetary matters. It was bank president Bendixen who declared that the fact that the German currency depreciated abroad during the war was "to a certain degree even desirable since this allows us the sale of foreign exchange at more attractive rates."

Eventually however, the reaction had to set in. The renunciation of the hostility towards theory of the historical school began. The decades of neglect of theoretical studies therefore led to the peculiar situation that today a foreigner, the Swede [Gustav] Cassel, has earned the gratitude of the German public for enlightening them about the problems and principles of the Germany economy. For example, Cassel has provided the German newspaper readers with the knowledge of the old purchasing power parity theory of exchange rates originally developed by Ricardo, as well as pointing out that unemployment as a continuing phenomenon must be a necessary consequence of the wage policy of trade unions. In his theoretical work, Cassel presents the teachings of

the subjective school, although he expresses himself somewhat differently and sometimes with a peculiar emphasis which is not quite worthy of imitation.

Although stragglers of the historical school are still trying to sing the old song of the end of the collapse of the marginal utility theory, one cannot avoid noticing that the writings of all younger economists—even in the German empire—contain more and more the ideas and thoughts of the Austrian school. The work of Menger and his friends has become the foundation of all modern economic science.\*

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\*[See also, Ludwig von Mises', *The Historical Setting of the Austrian School of Economics*. (New Rochelle: Arlington House, 1969)—ed.]



LUDWIG VON MISES was born in 1881 and has been recognized as the leading proponent of the "Austrian School of Economics" in the twentieth century. After studying with Eugen von Böhm-Bawerk, he received his doctorate degree from the University of Vienna in 1906. He taught at the University of Vienna (1913 & 1918-1938), was Economic Adviser to the Austrian Chamber of Commerce (1909-1934) and served as Director of the League of Nations' Austrian Reparations Commission (1918-1920). In 1927, he founded the Austrian Institute for Trade Cycle Research. Professor Mises also taught at the Graduate Institute for International Studies in Geneva (1934-1940) and at New York University (1945-1969). Among his important works are *The Theory of Money and Credit* (1912; revised ed., 1953), *Socialism* (1922; revised ed., 1951), *Liberalism [The Free and Prosperous Commonwealth]* (1927), *Monetary Stabilization and Cyclical Policy* (1928), *Critique of Interventionism* (1929), *Epistemological Problems of Economics* (1933), *Human Action, a Treatise on Economics* (1949; revised ed., 1966), *Theory and History* (1957), *The Ultimate Foundation of Economic Science: an Essay on Method* (1962) and *Notes and Recollections* (1978). Professor Mises died in 1973, at the age of 92.