

Office Hours: by appointment

Austrian Theory of the Market Process I

1.0 Course Description

This class is designed for advanced students of economics whose goal is to become a scholar in the fields of economics and political economy. Students will be exposed to the methodological arguments of the Austrian school of economics. We will also discuss the monetary theory, capital theory, and market process theory developed by the Austrian school. We will also discuss the critical arguments about the problems of interventionism and the impossibility of rational economic calculation under socialism. The political economy of liberalism and radical libertarianism will also be discussed in the end.

2.0 Course Readings

The readings for this course are divided into 3 groups: (1) background, (2) required, (3) recommended. The background reading is to set the stage for the discussion of the Post WWII development of the Austrian Theory of the Market Process. As you will see in the background reading, the Austrian school had a very rich history both pre-WWI and during the interwar period. In fact, in most history of economic thought treatments this would be the primary focus. And, indeed, a legitimate argument could be made that the interwar years were the years of “high theory” within the Austrian tradition culminating in the works of Mises and Hayek in the 1940s. It is during the 1930s and 1940s, that the debates with market socialism on the one hand, and with an emerging Keynesianism on the other took place. And it was during the 1930s and 1940s that the methodological battle lines between the Austrians and the positivists and formalists were clearly drawn. Moreover, there is an important pre-WWI history of the Austrian school that is just as important for the development of modern neoclassical economics. Carl Menger, Eugene Bohm-Bawerk, and Friedrich Wieser made fundamental contribution to value theory, production theory, and distribution theory that are still part of the core of economic teaching. Finally, Viennese intellectual culture at the beginning of the 20th century is recognized to be one of the most fertile that modern man has ever witnessed as major contributions were made not just in economics, but also in philosophy, psychology, mathematics, etc. Wittgenstein’s Vienna is a topic that fascinates and deserves serious study independent of one’s intellectual interest in the Austrian school of economics.

For background reading I have chosen two celebrated works in the modern history of economic thought. Bruce Caldwell’s *Hayek’s Challenge* (Chicago, 2003) is an intellectual biography of Hayek and contextualizes (as the title suggests) the development of Hayek’s ideas from his student days to his final writings in terms of the intellectual

debates he was involved with and the goals he set for his research program in the social sciences. Hayek had a vision, Caldwell identifies it, and then we learn of the trials and tribulations that Hayek faced in seeing that vision through. Along the way, we will meet several key figures in 20th century economics.

The second work in the modern history of economic thought you are expected to read is Phil Mirowski's *Machine Dreams* (Cambridge, 2008). Mirowski's book is a fun read in large part because of the "conspiracy theory" tone that is often evident. The book is deeply researched, and Mirowski's interpretative skills are considerable. But one should be forewarned that his bold conjectures about the role of the Cold War in shaping modern economics often come off as leaps of logic rather than razor sharp logical derivations. You are reading the book for two reasons: (a) it represents a bold reading of the development of post WWII modern economics, and (b) it is a reading that does give a considerable role played by Hayek in that development of information economics and mechanism design theory. Here you will read of Marschak, Koopmans, Arrow, and Hurwicz among others, and how their work in fundamental theory was inspired by the socialist calculation debate and Hayek's statement concerning the informational role of prices in coordinating economic affairs in a modern economy.

I also recommend that you read as many papers by Robert Leonard, whose book *Red Vienna* (Cambridge, forthcoming) has been anticipated for over a decade. Despite the delays in the work appearing in print, Leonard's papers are widely available on-line. His work is generally recognized as the most sophisticated intellectual history of economics of the Vienna period (see in particular his paper in *Isis*). But the central characters of his narrative are different than the standard accounts of the Austrian tradition. Instead of Mises, we learn of the mathematician Karl Menger (Carl Menger's son) and his influence on Oskar Morgenstern, and of both the philosophical and political activism of Otto Neurath. Neurath is a critical character in the subsequent development of the Austrian tradition because it was his ideas of the natural economy and the future of socialism that the economic calculation critique was in part directed at, and his ideas on positivism and the unity of science that the scientism critique was in part directed at. In the minds of Mises and Hayek, socialism and scientism were interconnected, and understanding this interconnection is critical to understanding the way they framed their contributions to both the methodology and method of modern economics in the 1940s and beyond.

You will note that I have not included any biography or background reading on Mises. There are several solid works on Mises, such as Eamonn Butler's *Ludwig von Mises: The Fountainhead of Modern Microeconomics* (Gower, 1988); Israel Kirzner, *Ludwig von Mises* (Intercollegiate Studies Institute, 2001); and Guido Huelsmann's *Mises: The Last Knight of Liberalism* (Mises Institute, 2007). For our purposes, the material that we need to discuss concerning Mises and his economics will already be discussed in the work of Leonard and Caldwell. And you already have a significant sum of pages to read prior to class as background and these works, especially Huelsmann's, wouldn't just significantly add to that total of pages, but actually come close to doubling it. However, I do encourage you to familiarize yourself with these works. Also, look up the various

writings of Richard Ebeling on Mises, and be alert to his biography on Mises that is supposed to be published in 2010.

It is my expectation that you will have read Caldwell, Mirowski and Leonard (*Isis* article) prior to our first class meeting on August 31st.

The required readings for this class consist of Mises's *Human Action*; Hayek's *Individualism and Economic Order*; Rothbard's *Man, Economy, and State*; and Kirzner's *Competition and Entrepreneurship*. These works represent the fullest statements of the post-WWII development of Austrian economics from 1950 to 1975. In the narrative that I am constructing, Mises and Hayek in their own respective ways made major theoretical innovations in the 1940s which were presented in *Human Action* and *Individualism and Economic Order*. Rothbard and Kirzner in their own respective ways were responsible for restating those innovations to a new generation of economists and in so doing provided the foundations of modern Austrian economics.

You are expected to not just read these works, but to master these texts in the same way that you were expected to master the texts of Mas-Colell in microeconomics or David Romer in macroeconomics. If you want to be an Austrian economist, then you need have to know these works by Mises, Hayek, Rothbard, and Kirzner.

Recommended readings will come in two groups. The first group will be journal articles and chapters from books that are written by post 1975 scholars in the Austrian tradition. These will be scattered throughout the syllabus and should point you in the right direction. The second group will be books by modern scholars outside of the Austrian tradition who are making arguments that are either traditionally associated with the Austrian school or consistent with the Austrian school.

The list of recommended books include: Cristina Bicchieri, *The Grammar of Society* (Cambridge, 2005); Tyler Cowen, *Discover Your Inner Economist* (Dutton, 2007) and Tyler Cowen, *Create Your Own Economy* (Dutton, 2009); Jon Elster, *Explaining Social Behavior* (Cambridge, 2007); Roman Frydman and Michael Goldberg, *Imperfect Knowledge Economics* (Princeton, 2007); Avner Greif, *Institutions and the Path to the Modern Economy* (Cambridge, 2006); Russell Hardin, *Indeterminacy and Society* (Princeton, 2005) and Russell Hardin, *How Do You Know?* (Princeton, 2009); Richard Posner, *A Failure of Capitalism* (Harvard, 2009); Douglass North, John Wallis and Barry Weingast, *Violence and Social Order* (Cambridge, 2009); Paul Seabright, *The Company of Strangers* (Princeton, 2005); and Andrei Shleifer, *Inefficient Markets* (Oxford, 2000).

This list is certainly not meant to be a comprehensive list of contemporary works that are relevant to the interests of economists interested in the Austrian school. But they raise many of the methodological, analytical, empirical, and social philosophical issues that were raised in the works of Mises, Hayek, Rothbard and Kirzner. In short, there is a broader conversation going on in economics and political economy that contemporary students of the Austrian school should be aware of, and contributing to, and this list of works has been given to point you in that direction.

The first 10 weeks of the class will be devoted to learning the foundations of modern Austrian economics and its further development since 1975 by scholars in the tradition, and the last 5 weeks of the class will be devoted to engagement with the latest thinking in social science methodology and economic theory, and a discussion of the future directions of research inspired by the Austrian tradition of economic scholarship.

3.0 Grading Policy

Grading policy for this class is based on 3 grades. Class participation (perhaps periodic quizzes), research paper on a topic of your choosing, and a take-home final that is designed to help you prepare for the field exam. Each will be equally weighted in determining the final grade for the class.

4.0 Lectures

DATE	TOPIC	READING
August 31	Austrian Economics in the Contemporary Intellectual Landscape of Economics	Caldwell, especially 133-319. Mirowski, especially 232-308. Leonard, <i>Isis</i> (1998).
September 7	LABOR DAY	
September 14	The Methodology of the Austrian School of Economics	Mises 1-142. Hayek 1-76. Rothbard 1-200, especially 1-66. Kirzner 1-85, especially 3-7; 32-37. Caldwell 17-130; 232-260; 407-408.
September 21	The Positive Economics of the Market Economy of the Austrian School	Mises 232-397. Hayek 77-106. Rothbard 201-272; 560-660. Kirzner 1-29; 88-134. Caldwell 370-405.
September 28	Factor Pricing and the Process of Production	Mises 479-523. Hayek 77-91. Rothbard 273-559. Kirzner 135-211.
October 5	Economic Calculation: <i>The Austrian Contribution</i>	Mises 200-231; 689-715. Hayek 119-208. Rothbard 542-550; 830-832. Kirzner 212-242. Boettke 1998.
Tuesday, October 13	The Dynamics of Interventionism	Mises 716-861. Rothbard 765-890. Boettke 1993. Ikeda 1997. Kurrild-Klitgaard, ed., 2005.

October 19	Profits, Interest and Investment	Mises 538-586. Hayek 220-254. Rothbard 661-764; 850-879. Salerno, ed., 2008.
October 26	The Battle with Keynes and Keynesian Economics	Caldwell 150-181. Garrison 1985; 1993; 2005. Caldwell, ed. 1995.
November 2	The Entrepreneurial Market Process and the Role of Equilibrium Theorizing in Economics	Mises 257-326. Hayek 33-56; 92-106. Rothbard 468-501. Kirzner 1-134. Kirzner 1990. Boettke 1997.
November 9	Methodology in a Post-Positivist Age	Elster. Hardin 2005. Leeson and Boettke 2006. Boettke 2010.
November 16	The Economics of Time and Ignorance	Frydman and Goldberg. Hardin 2009. Cowen 2007. Boettke 2002. O'Driscoll and Rizzo 1985. Koppl 2006.
November 23		
November 30	The Financial Crisis and Economic Theorizing	Posner. Shleifer. Garrison 2009a; 2009b; 1989. White 2008 and 2009. Horwitz 2000.
December 7	How Far Can Spontaneous Order Be Stretched? Research paper due	Mises 143-176. Hayek 255-272. Rothbard 80-87, especially 85. Bicchieri. Seabright. Greif. North, et. al.
December 14	FINAL EXAM Submission deadline: 7:15pm	

5.0 Field Exam and Beyond in Austrian Economics

The final exam in this class is designed to help you practice for the field exam offered in Austrian Economics. To qualify to take the exam you must also successfully complete The Theory of the Market Process II (Econ 881), which will be taught by Professor Wagner in the Spring 2010.

The Austrian School of Economics has its own JEL code – B53. This comes under the heading of heterodox approaches to economics. While it is important for a research field

to have its own JEL code, I am not sure the designation “heterodox” is the best intellectual home for Austrian economics. But as you develop in your career you will have to make that decision for yourself.

As you will see throughout the course one of the distinguishing characteristics of the Austrian school from Menger to today is the striving for a level of philosophical awareness and sophistication which is simply absent from most other economists. If you look at the label “Austrian Economics”, then you can see that individual scholars choose which of the terms to emphasize. If you are doing Austrian economics, then the methodological and unique philosophic context within which these ideas about human action and exchange relationships tends to get emphasized. If, on the other hand, you are doing Austrian economics, then the analytical ideas about human action and exchange relationships, and the common ground with other economists tends to get emphasized. If it is the Austrian element that fascinates you, then you should be drawn to understanding the ideas of Husserl, Schutz, and even Wittgenstein. If it is the economic element that fascinates you, then you should be drawn to understanding not just fellow travelers*, but Walras, Samuelson, Arrow, and Stiglitz. To most Austrian economists, both sides tend to fascinate them, but they have to figure out the balance of their research interests. In my experience, my generation of Austrian economists tended to emphasize the Austrian elements, while the most recent generation of Austrian economists have tended to emphasize the economic elements.

There are 3 specific journal publishing outlets in Austrian economics: *Review of Austrian Economics*; *Quarterly Journal of Austrian Economics*; and *Advances in Austrian Economics*. There are also several book series that publish works that are focused on Austrian economics, the most prominent being “Foundations of the Market Economy” series with Routledge. If you are going to work in the field, then you should be intimately familiar with the work in these journals and in that series.** However, I want to stress again, that there are opportunities to publish Austrian-relevant research in the top journals and with the top university presses.

And, it is important to stress to aspiring economists why publishing in those top journals and respected presses matters. This is not about career advancement, though obviously if

* The list of important fellow travelers who have influenced greatly the subsequent development of Austrian ideas would include: Wicksell, Wicksteed, Knight, and Robbins, prior to WWII, and after WWII, Alchian, Bauer, Buchanan, Coase, Demsetz, Leijonhufvud, North, Olson, Schelling, Shackle, V. Smith, Tullock, Williamson, and Yeager. With my recommended readings I am suggesting that the list is ever expanding in the 21st century; especially when you consider my omission of such obvious choices as William Easterly and Timur Kuran. In other words, in my opinion the ideas of Mises and Hayek are being discussed everywhere one looks in the contemporary literature so opportunities for professional engagement abound in philosophy, politics, economics, business studies, etc.

** I would also stress that you should read the Presidential Addresses of the Society for the Development of Austrian Economics since its founding: Karen Vaughn (1997), Mario Rizzo (1998), Charles Baird (1999), Peter Lewin (2000), Peter Boettke (2001), William Butos (2002), Steve Horwitz (2003), Roger Garrison (2004), Roger Koppl (2005), Sanford Ikeda (2006), Randall Holcombe (2007), and Joseph Salerno (2008). All of these addresses are available electronically through the *RAE* except for Vaughn’s (published in *AAE*) and Salerno’s is forthcoming.

you succeed a solid career will be forged. It is about tracking truth as you see it, and then maximizing your readership and scholarly/scientific impact. Even if you believed that Mises and/or Hayek had the last word on scientific advancement in economic reasoning, then you will want to get their ideas into as many key hands within the economics profession as possible. Success, then, would be measured the same way one would measure a mainstream career trajectory. Publication in the best journals and with the most respected presses; positions at the higher ranked departments; professional awards from the most prestigious societies, etc. The idea of an alternative sub-culture within the economics profession that can be successful without eventually translating into those more traditional measures of scientific impact and success is pure fantasy and in fact one of the most counter-productive habits of thought to have infiltrated the Austrian school of economics in the late 20th century. You should not aspire to publish in the *RAE*, but instead the *AER*. Just a shift of a few letters, but a world of difference it would make.

This should not be seen as argument for disregarding the publishing that takes place in the *RAE*, *QJAE*, and *AAE*, or with Routledge (or Elgar, or Mises Institute, etc.). As someone who has decided to build a professional expertise in Austrian economics you must not only read these works, but contribute to this literature. But what I am arguing is that if this literature is successful, it will become more relevant to the research product one sees in more widely recognized publication outlets. As an aspiring economist, what you want is for your efforts at truth-tracking to be so insightful that they are viewed as a productive input into the productive process of truth-tracking by other economists. This is how scientific progress is made, and careers are built.

It is a fascinating time to be an economist. The world around us begs for economic understanding and explanation. The professional discourse similarly is seeking new and fresh ideas in economics and political economy. The intellectual endowment provided by Mises and Hayek is a rich one to work with.

Becoming an economist should be the most amazing intellectual adventure of your life. Pursue it with passion.

Good luck.