

Professor Peter J. Boettke  
Econ 880/Fall 2022  
W 4:30-7:20  
D-100 Buchanan Hall

## The Theory of the Market Process I

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

- Ludwig von Mises, *Human Action*

This course will be organized around the theme of the Austrian School of Economics as developed by Israel Kirzner in the second half of the 20<sup>th</sup> century. We will be utilizing several selections from Kirzner's *Collected Works* to frame our discussion of the modern and contemporary Austrian School. The Austrian School of Economics can be usefully thought of as consisting of 4 periods. The founding period will be represented by Carl Menger, Eugen Bohm-Bawerk and Frederic Wieser. The development phase will be represented by Ludwig von Mises, Joseph Schumpeter and F. A. Hayek. The modern phase will be Murray Rothbard, Israel Kirzner and Ludwig Lachmann. And, the contemporary period will be represented by the work of Don Lavoie, Mario Rizzo, Lawrence White and others.

The Austrian School of Economics has a long and distinguished history as significant contributors to what I have dubbed mainline economics. Paul Samuelson, e.g., in his obituary of Swedish economist Bertil Ohlin, decided to play the game of "what if" -- in this case, "what if the Nobel Prize was established in 1900, then who would have won the prize between 1901 and 1930?" This is list of names Samuelson (1981) thinks would have won the prize:

One cannot forbear playing the game of might-have-been. Here is the most likely scenario of awards from 1901 on: **Bohm-Bawerk**, Marshall, J.B. Clark, Walras, and *Wicksell*; **Carl Menger**, Pareto, *Wicksteed*, Irving Fisher, and Edgeworth; Sombart, Mitchell, Pigou, Adolph Wagner, Allyn Young, and *Cannan*; *Davenport*, Taussig, **Schumpeter**, Veblen, and Bortkiewicz; Cassel, J. M. Keynes, Heckscher, J. R. Commons, and J. M. Clark; Hawtrey, **von Mises**, Robertson, H. L. Moore, and *F. H. Knight*.(p. 358, n1)

I have marked in **bold** the members of the Austrian School of Economics in his list, however, in this same list I have *italicized* those that were particularly close in substance to the Austrians though not part of the Viennese intellectual community. And, I am probably missing cross

influences, and the cut off for Samuelson's thought experiment was 1930, so he does not have Hayek or Lionel Robbins listed, let alone Fritz Machlup and Oskar Morgenstern, all of whom made their major contributions after 1930. By this accounting, not only is the Austrian School of Economics distinctive, it's practitioners are *distinguished contributors* to the scientific conversation in economics, political economy and social philosophy throughout the 20<sup>th</sup> and I am going to argue into the 21<sup>st</sup> century.

In my own work, I have come to contrast mainline economics with mainstream economics, where mainline refers to the foundational principles of economics and continuity in the development of those core principles from Adam Smith to contemporary thinkers, whereas mainstream refers to whatever is currently fashionable among so-called elite economic thinkers at any point in time. Sometimes the mainline is the mainstream, but at other times, the mainstream deviates significantly from the mainline, and it is precisely at these moments of disjoint that often schools of thought emerge in economics to stress the necessity of core fundamental principles. In my reading of the history of political economy, the mainline of economics is connected to invisible hand reasoning, and, in particular, is related to the theoretical effort to derive the invisible hand proposition from the rational choice postulate *via* institutional analysis. In this way, the pure logic of choice is married with situational logic to produce both economic theory and its application to render intelligible the operation of commercial society.

From this perspective, the Austrian School of Economics is a branch of neo-classical economics, but from Menger onward subtle differences in the way the principles of economics were understood and presented were evident. So evident are these subtle differences, in fact, that the Austrian School of Economics has been recognized as unique since its founding 150 years ago. Menger is recognized as one of the three scientific innovators that produced the Marginal Revolution, but his consistent subjectivism set him apart from Jevons and Walras.

As background, you might find it helpful to read the following historical treatments of the Austrian School, or at least synopsis of these works and/or reviews that are accessible. First, Erwin Dekker's *The Viennese Students of Civilization*. Second, Karen Vaughn's *Austrian Economics in America*. And, third, Janek Wasserman's *Marginal Revolutionaries*. This exercise will be important to historically situate the Austrian School in the literature on the history of economic thought. Furthermore, to familiarize yourself with the main contributions of the Austrian School, I would also suggest consulting the following reference volumes I have edited: (1) *Elgar Companion to Austrian Economics* (1994); (2) *The Handbook of Contemporary Austrian Economics* (2010); and *The Oxford Handbook of Austrian Economics*, with Chris Coyne (2015). These books will be valuable throughout the term (and in fact your career) as reference works, but there really is no substitute for the original works themselves.

## Required Reading

The foundational texts for the class are Mises's *Human Action* (1949) and Hayek's *Individualism and Economics Order* (1948). I will not give page references to these works, so make use of the table of content and index to match with the topic of the week. Assume that each week there are

foundational concepts that were developed in these two texts that are being worked on in the subsequent literature.

We will then focus on how the Mises-Hayek paradigm is developed in the work of Kirzner, namely *The Economic Point of View* (1960), *Market Theory and the Price System* (1963), *An Essay on Capital* (1966), *Competition and Entrepreneurship* (1973), and *Discovery, Capitalism and Distributive Justice* (1989). We will also look at the work of James Buchanan during this same period, including his classic work *Cost and Choice* (1969) and various essays of his in the 1950s-1970s that touch on the theme of the exchange paradigm versus the allocation paradigm in economics that are in Vol 1 of his *Collected Works*. We will then draw on works from contemporary Austrian economists such as Dom Armentano's *Antitrust and Monopoly* (1981), Lawrence White's *Free Banking in Britain* (1984), Don Lavoie's *Rivalry and Central Planning* (1985a) and *National Economic Planning: What is Left?* (1985b), George Selgin's *A Theory of Free Banking* (1988), Steve Horwitz's *Microfoundations and Macroeconomics* (2000), and Gerald O'Driscoll and Mario Rizzo's *Austrian Economics Re-Examined* and Rizzo and Glenn Whitman's *Escaping Paternalism* (2020).

## **Class Format**

Each week we will have a lecture running roughly 1 hour to 1 hour and 15 minutes, followed by break and then open discussion for the remainder of the class. I am also looking to post lectures and video clips and podcasts on blackboard in the hope of moving more toward less lecture and more classroom discussion.

## **Grading Policy**

We will have 3 sources for your course grade. Four essays 6-8 double spaced pages that will be assigned throughout the term. A research paper that you are working on to submit to a peer-reviewed journal, such as *Review of Austrian Economics*. There will also be a take home final exam consisting of 5 questions that will be designed to prepare you for the field exam if you so choose to pursue that path in your graduate career.

The short essays will constitute 25%, final exam 25% and the research paper 50% of your final grade.

I do expect active and engaging participation from all in this class. To reiterate this is a graduate level economics course in a specialized sub-field. Be ready to contribute.

## **Course Objectives**

Upon completion of this course, you will:

- Understand the foundational contributions of the Austrian School of Economics

- Understand the major strands of academic literature in Austrian Economics in methodology, analytics, and applications to political economy and public policy
- Be able to synthesize existing ideas in the field of Austrian Economics and build on these ideas to generate novel contributions to this literature
- For MA students – be able to apply the core concepts in Austrian Economics to current events
- For PhD students - be able to write academic papers in the field of Austrian Economics suitable for peer review.

## Course Schedule

Date	Topic	Readings
Aug 24 <sup>th</sup>	Course Introduction: The Austrian Contribution to Economic Science, Political Economy and Social Philosophy	
August 31 <sup>st</sup>	The Evolution of Economic Science	Kirzner, <i>The Economic Point of View</i> (1960): 1; 4; 6-7
Sept 7 <sup>th</sup>	Value, Costs, Prices	Kirzner, <i>Market Theory &amp; the Price System</i> (1963): 1; 4; 6; 9 Buchanan, <i>Costs &amp; Choice</i> (1969)
Sept 14 <sup>th</sup>	Economics as a Coordination Problem	Kirzner, <i>Market Theory &amp; the Price System</i> (1963): 3; 7; 11; 13
Sept 21 <sup>nd*</sup>	Development Economics Lant Pritchett 2:00-3:30pm	
Sept 28 <sup>th</sup>	Market Process Theory	Kirzner, <i>Competition &amp; Entrepreneurship</i> (1973): 1-3; 4; 6 Buchanan, <i>CW Vol. 1</i> : 28-42; 244-245; 260-277
Oct 5 <sup>th</sup>	MPS Meetings in Oslo, Norway	
Oct 12 <sup>th</sup>	Profits, Interest and Investment	Kirzner, <i>Essays on Capital and Interest</i> (1966): Essay 2
Oct 19 <sup>th</sup>	Socialist Calculation Debate	Lavoie (1985a): 1-7; (1985b): 2-3
Oct 26 <sup>th</sup>	Market theory and public policy	Kirzner, <i>Competition &amp; Entrepreneurship</i> (1973): 3; 6 Armentano, <i>Anti-Trust and Monopoly</i> (1981): 1; 3-5; 9 O'Driscoll and Rizzo <i>Austrian Economics Re-Examined</i> (2015): 6-7

Nov 2 <sup>rd</sup>	Money and Macro	Horwitz (2000): 1-8
Nov 9 <sup>th</sup>	Alternative Monetary Institutions	White (1984): 1-6. Selgin (1988): 1-9; 11
Nov 16 <sup>th</sup>	Monetary Theory, Monetary Policy, and Public Policy	Boettke, Salter and Smith (2021) <i>Money and the Rule of Law</i>
Nov 23 <sup>rd</sup>	Thanksgiving break	
Nov 30 <sup>th</sup>	Political Economy	Kirzner, <i>Discovery, Capitalism and Distributive Justice</i> (1989): 1; 3; 6-7 Buchanan, CW Vol. 1: 45-59; 75-102; 191-209; 455-468 Lavoie (1985b): 7 Rizzo and Whitman (2020): 1; 6-9
December 7 <sup>th</sup>	Course Conclusion: What is the Austrian School of Economics Today?	O'Driscoll and Rizzo (2015): Part I-Part II; chapter 10; Part IV-Part V