Acting Man and Economics

06/19/2018 • Ludwig von Mises

People generally believe that economics is of interest only to businessmen, bankers, and the like and that there is a separate economics for every group, segment of society, or country. As economics is the latest science to have been developed, it is no wonder that there are many erroneous ideas about the meaning and content of this branch of knowledge.

It would take hours to point out how common misunderstandings developed, which writers were responsible, and how political conditions contributed. it is more important to enumerate the misunderstandings and discuss the consequences of their acceptance by the public.

This first misunderstanding is the belief that economics does not deal with the way men really live and act, but with a specter created by economics, a phantom that has no counterpart in real life. The criticism is made that real man is different from the specter of the "economic man." once this first misunderstanding is removed, a second misunderstanding arises—the belief that economics supposes that people are driven by one ambition and intention only—to improve their material conditions and their own well-being. Critics of this belief say that not all men are egoistic.

A third misunderstanding is that economics assumes all men to be reasonable, rational, and guided by reason only, while in fact, the critics maintain, people may be guided by "irrational" forces.

These three misunderstandings are based on entirely false assumptions. Economics does not suppose that economic man is different from what man is in everyday life. *The only supposition of economics is that there are conditions in the world with regard to which man is not neutral, and that he wants to change the situation by purposeful action*. So far as man is neutral, indifferent, content, he takes no action, he does not act. But when a man distinguishes between states of various affairs and sees an opportunity to improve conditions from his point of view, he acts.

Action is the search for improvement of conditions from the point of view of the personal value judgments of the individual concerned. This does not mean improvement from a metaphysical view, nor from God's point of view. Man's aim is to substitute what he considers a better state of affairs for a less satisfactory one. He strives for the substitution of a more satisfactory state of affairs in place of a less satisfactory state of affairs. And in the satisfaction of this desire, he becomes happier than he was before. This implies nothing with reference to the content of the action, nor whether he acts for egoistic or altruistic reasons.

To eliminate the misunderstanding that arises when a distinction is attempted between

"rationalism" and "irrationalism," it must be realized that what man does consciously is done under the influence of some force or power which we call reason. Any action aimed at a definite goal is in this sense "rational." The popular distinction between "rational" and "irrational" is entirely without meaning. Examples of "irrationalism" cited are patriotism or the purchase of a new coat or a symphony ticket when something else might have appeared a more sensible action. The theoretical science of human action presupposes only one thing—that there is *action*, i.e., the conscious striving of individuals to remove uneasiness and to substitute a more satisfactory state of affairs for one that is less satisfactory. No judgment of value is made as to the reason or content of the action. Economics is neutral. Economics deals with the results of value judgments, but economics itself is neutral.

Nor is there any sense in trying to distinguish between "economic" and "non-economic" actions. Some actions deal with the preservation of man's own vital senses and necessities—food, shelter, and so on. Others are considered to be driven by "higher" motivations. But the value placed on these various goals vary from man to man, and differ for the same man from time to time. Economics deals merely with the action; it is the task of history to describe the differences in goals.

Our knowledge of economic laws is derived from reason and cannot be learned from historical experience because historical experience is always complex and cannot be studied as in a laboratory experiment. *The source of economic facts is man's own reason*, i.e., which we call in epistemology *a priori* knowledge, what one knows already; *a priori* knowledge is distinguished from *a posteriori* knowledge, knowledge which is derived from experience.

Regarding *a priori* knowledge, the English philosopher John Locke [1632–1704] developed the theory that the human mind is born a blank slate on which experience writes. He said there was no such thing as inherent knowledge. Gottfried Wilhelm von Leibniz [1646–1716], a German philosopher and mathematician, made an exception in the case of the intellect itself. According to Leibniz, experience does not write on empty white pages in the human mind; there is a mental apparatus present in the human mind, a mental apparatus that does not exist in the minds of animals, which makes it possible for men to convert experience into human knowledge.

I am not going to enter into the argument between "rationalism" and "empiricism," the distinction between experience and knowledge, which the British philosopher and economist John Stuart Mill [1806–1873] called *a prioristic* knowledge. However, even Mill and the American pragmatists believed that *a prioristic* knowledge comes in some way from experience.

The way in which economic knowledge, economic theory, and so on relate to economic history and everyday life is the same as the relation of logic and mathematics to our grasp of the natural

sciences. Therefore, we can eliminate this anti-egoism and accept the fact that the teachings of economic theory are derived from reason. Logic and mathematics are derived in a similar way from reason; there is no such thing as experiment and laboratory research in the field of mathematics. According to one mathematician, the only equipment a mathematician needs is a pencil, a piece of paper, and a wastebasket—his tools are mental.

But, we may ask, how is it possible for mathematics, which is something developed purely from the human mind without reference to the external world and reality, to be used for a grasp of the physical universe that exists and operates outside of our mind? Answers to this question have been offered by the French mathematician Henri Poincaré [1854–1912] and physicist Albert Einstein [1879–1955]. Economists can ask the same question about economics. How is it possible that something developed exclusively from our own reason, from our own mind, while sitting in an armchair, can be used for a grasp of what is taking place on the market and in the world?

The activities of every individual—all actions—stem from reason, the same source from which come our theories. Man's actions on the market, in the government, at work, at leisure, in buying and selling, are all guided by reason, guided by choice between what a person prefers as against what he does not prefer. Reason is the method by which a solution (whether good or bad) is reached. *Every action can be called an exchange insofar as it means substituting one state of affairs for another.* Hopefully the actor is substituting a situation he prefers for one which he likes less.

The starting points for the natural sciences are the various facts established by experiment. From these facts, theories are built to more and more abstractions, to more and more generalities. Final theories are so abstract that they are practically inaccessible to the general multitude. That doesn't make them less valuable; it is enough that they are accessible to the few scientists.

In an *a prioristic* science, we start with a general supposition—*action is taken to substitute one state of affairs for another*. This theory—meaningless to many—leads to other ideas that become more and more understandable and less abstract.

Natural sciences progress from the less general to the more general; economics proceeds in the opposite direction. Natural sciences are in a position to establish constant relations of magnitude. In the field of human action, no such constant relations prevail, so there is no opportunity for measurement. The value judgments which spur men to act, which lead to prices and market activity, do not measure; they establish distinctions of degree; they grade. They do not say "A" is equal to, or is more or less than "B." They say, "I prefer A to B." They don't establish judgments. This has been misunderstood for 2000 years. Even today there are many persons, even eminent philosophers, who misunderstand this completely. It is from the system of values and preferences that the price system of the market arises.

of the market arises.

Aristotle wrote, among other things, about the various attributes of men and women. He was often mistaken. Had he asked Mrs. Aristotle about women, he would have found he was mistaken in some respects; he would have learned differently. He was also mistaken in stating that if two things were to be exchanged on the market, they must have something in common, that they were being exchanged because they were equal. Now if they were equal, why was it necessary to exchange them? If you have a dime and I have a dime, we don't exchange them because they are the same. It follows, therefore, that if there is an exchange, there must be some inequality in the items being traded, not equality.

Karl Marx [1818–1883] based his theory of value on this fallacy. In *Capital and Interest*, by Eugen von Böhm-Bawerk [1851–1914], see Chapter XII dealing with Marx ("The Exploitation Theory" in Volume I, H*istory and Critique of Interest Theories*). Long after Marx, Henri Bergson, in a much-admired book about the two sources of morals in religion, accepted the same fallacy—if two things are exchanged on the market they must be equal in some way. But things that are "equal" are not exchanged; exchanges take place only because things are *unequal.* You take the trouble of going to the market because you value the loaf of bread more highly than the money you give for it. People exchange things because at that time they prefer other things to money. An exchange *never* occurs with the *intention* of a loss. The acting man is never pessimistic because his action is inspired by the idea that conditions can be improved.

The aim of action is to substitute a state of affairs better suiting the men taking the action than the previous situation. The value of any change in their situation is called a "gain" if it is positive, a "loss" if it is negative. This value is purely psychic, it cannot be measured. You can say only that it is greater or less. It becomes measurable only insofar as things are exchanged on the market against money. As far as the action itself is concerned, it has no mathematical value.

But, you say, this contradicts our daily experience. Yes, because our social environment makes calculations possible insofar as things are exchanged for a common medium of exchange, money. When things are exchanged against money, it is possible to use monetary terms for economic calculations, but only when three conditions are filled:

1. There must be private ownership, not only of the products, but also of the means of production;

2. There must be division of labor and, therefore, production for the needs of others;

3. There must be indirect exchange in the terms of a common denominator.

By and large, given these three conditions some mathematical values may be established, although

By and large, given these three conditions some mathematical values may be established, although not precisely. These measurements are not exact because they deal with what took place yesterday, historically. Business financial statements may look precise, but even the money value of an inventory entered at "so many dollars" is a speculative value of future anticipations; the value credited to equipment and other assets also is speculative. The real problem of inflation is that it falsifies these calculations and brings about tragic problems.

Monetary calculations do not necessarily exist in all kinds of organizations or societies. They did not exist when economics began. The earliest humans acted; humans have always acted; but it was thousands of years before the evolution of the division of labor and of a financial apparatus made monetary calculations possible. Monetary calculations developed step by step during the Middle Ages. In their early development they lacked many features we think of today as necessary. (In a socialist system, these conditions would again disappear and make such calculations and measurements impossible.)

The quantitative nature of the natural sciences enables mechanics to make plans and build bridges. If you know what must be built, technology based on the knowledge of the natural sciences is sufficient. The questions are, however: What should be constructed? What should be done? Technologists cannot answer these questions.

In life the materials of production are scarce. No matter what we do there will always be other projects for which the necessary factors of production cannot be spared. There will always be other urgent demands. This is the factor that businessmen take into account in calculating loss and success. When a businessman decides against a certain project because the cost is too high, it means the public is not prepared to pay the price to use raw materials in that manner. Use is made of the available factors of production for the realization of the greatest number of those projects that satisfy the most urgent needs without wasting factors of production by withdrawing them from more urgent to less urgent employment.

To establish this it is necessary to be in a position to compare the outlays of various factors of production. For example, let it be assumed that it is necessary to build a railroad between two towns —A and B. Let us assume that there is a mountain between A and B. There are three possibilities—to go over, through, or around the mountain. A common denominator is necessary to calculate the comparative value. But this can give only a picture of the monetary situation; it is not a measurement. It is an evaluation in the light of present-day needs and situations. Tomorrow conditions will be different. The success or failure of every business project depends upon its success in anticipating future possibilities.

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The problem with trying to develop a quantitative science of economics is that many persons imagine that theoretical economics must follow the evolution of other branches of science. The natural sciences developed from being qualitative to being quantitative in nature and many people are inclined to believe that the same trend must take place in economics also. However, there are no constant relationships in economics, so no measurement is possible. And without measurement, the quantitative development of economics cannot take place. Quantitative facts in economics belong to economic history—not to economic theory.

A book titled *Measurement of the Elasticity of Demand* was reviewed recently by a man now in the U.S. Senate, Paul Douglas [1892–1976], who may even be hoping for higher political office sometime. Douglas said economics should become an exact science with fixed values like atomic weights in chemistry. But this book itself does not refer to fixed values; it refers to the economic history of one definite period of time in one particular country, the United States. The results would have been different if another period of time or if another country had been considered. Within the framework of the universe in which we operate, atomic weights do not change from one period of time or from one country to another. On the other hand, economic values and economic quantities do change from time to time and from place to place.

Economics is the theory of human action. It is a historical fact of great importance, for example, that the usefulness of the potato was discovered by the natives of Mexico, brought to Europe by a British gentleman, and that its use spread all over the world. This historical fact has had important effects on Ireland, for instance, but from the point of view of economic theory it was just an accident.

When you introduce figures into economics you are no longer in the field of economic theory, but in the field of economic history. Economic history is also, of course, a very important field. Statistics in the field of human action is a method of historical study. Statistics give a description of a fact, but they cannot prove any more than that fact. (It is true that some statisticians are "swindlers" and, as a matter of fact, some statisticians in the government were probably appointed merely for that purpose.)

Some people may misinterpret these statements and conclude that the purpose of economics, being a purely *a prioristic* science, is to develop a program for a future science, and that economics is a theory practiced only by "armchair gentlemen." Both these statements are wrong. Economics is not a program for a science that doesn't yet exist. And it is not a science merely for purists. Therefore, we must reject the ideas of some people that one must learn history to study human action. History is important. But you cannot deal with present-day conditions by studying the past. Conditions change.

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As an example of what I mean: The National Bureau of Economic Research published a report on the subject of installment selling which appeared on the eve of World War II, on the eve of inflation, and on the eve of government credit restrictions. At the moment when the study was made, it was already "dead"; it dealt with matters that were already past. I don't mean to say that it was useless. With good brains one can learn a lot from it. But don't forget it is not economics—it is economic history. What they were really studying was the economic history of the most recent past.

Darwin realized this too. He saw that in studying animals, the animal was killed at the moment when it was dissected for study, so that one could never actually study the animal—one can never study life itself.

The same is true of economics. One cannot describe the present economic system—one can only describe the past. One cannot predict about the future as a result of studying the past. Very often economic historians teach history under the label of "economics." Even though you know everything about the past, you know nothing about the future.

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Meet the Author

Ludwig von Mises

Ludwig von Mises was the acknowledged leader of the Austrian school of economic thought, a prodigious originator in economic theory, and a prolific author. Mises's writings and lectures encompassed economic theory, history, epistemology, government, and political philosophy. His contributions to economic theory include important clarifications on the quantity theory of money, the theory of the trade cycle, the integration of monetary theory with economic theory in general, and a demonstration that socialism must fail because it cannot solve the problem of economic

calculation. Mises was the first scholar to recognize that economics is part of a larger science in human action, a science that he called *praxeology*.

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