Herbert Davenport

©J. Patrick Gunning
Visiting Professor
U.S. Coast Guard Academy
Management Department
15 Mohegan Avenue
New London, CT 06320

Send feedback:
Email: gunning@nomadpress.com
Go to Pat Gunning's Pages

Herbert Joseph Davenport (1861-1931) was a self starter whose academic career began before he entered the Ph.D. program at the University of Chicago in 1897, which he completed in one year. The earliest roots of his ideas seem to be the subjectivism of the 19th century French subjectivists, which he learned during a brief one-year stint abroad (1890-91) as a university student. Later, he was influenced by the subjectivism of the early Austrian school. More complete biographies are available (Dorfmann, 1949; Newman, 1952; Homan, 1931). The focus here is on his contributions to economics.

His career as a major contributor to economics began with his 1894 essay on subjective opportunity cost and ended, arguably, with his *Economics of Enterprise* (1914), a book on the theory of markets and prices. He later served on the faculty of Cornell University and as president of the American Economic Association. He established a reputation as an international scholar with his *Value and Distribution* (1908), which contained a highly-informed critical history of contemporary economic thought from the classical period to the start of the 20th century (Fisher, 1908).

Two characteristics distinguished the theory of markets and prices in his 1914 book from that of other writers: his consummate subjectivism and his effort to purge price theory of value elements. His subjectivism involves simultaneously viewing markets and prices from three perspectives. The first consists of those of the individual transactors. The second is the perspective of the single-minded onlooker who does not think beyond the actors in the specific markets within his immediate purview. The third is the perspective of the economist who tries to conceive of a complete interdependent economic system with the help of an analogy with the actions of a hypothetical isolated actor (1914: Ch. 6). At some point prior to writing his 1914 book, he recognized that the extreme difficulty of building an image of markets and prices incorporating these three perspectives can only be overcome by concentrating the market economy's driving force into a single function-performing role – the entrepreneur. Thus, Davenport was led to describe the economic system mainly in terms of the entrepreneur role. This logical yet crucially important extension of his 1984 article transformed what he perceived initially as subjective opportunity cost into "entrepreneurs' cost" (1914, Ch. 6 and Ch. 8). This "entrepreneur view" of markets and prices is the hallmark of non-mathematical approaches to the system of markets and prices. Davenport deserves credit for inventing it and, in so doing, making a seminal contribution to the Austrian theory of value and cost.

Davenport was one of several pioneers who recognized that because the entrepreneur is

forward looking, she treats all factors of production in the same way – as potential contributors to profit. This led him to follow the early Austrians and, in some measure, J. B. Clark in rejecting the classical tripartite division of the factors of production. From the entrepreneur view, assets are evaluated according to their prospective contribution to profit, not their material characteristics or origin. This same perspective put him in a camp with Frank Fetter and Irving Fisher, who defined wealth in terms of the appraisement factors of production and goods by means of a capitalization process.

Davenport attempted to purge values from economics by asserting first that market theory includes as final goods all things that have a price, regardless of how objectionable they may be to common sensibilities. Second, it includes as resources all actions and things that an individual may regard as productive of income, regardless of whether others are harmed by them. This includes, for example, polluting behavior and burglary tools. Thus, for Davenport, the starting point was not the pure market economy, as it is in most of modern microeconomics. It was, as in the case of Ronald Coase, the market economy as it is – or as Davenport saw it. To judge whether the market economy, as it is, contributes to "welfare" in relation to other systems requires a separate judgment that lies outside the realm of economics (1914, Ch. 17). Whereas the utilitarian may be inclined to begin his market theory with an image of a pure market economy in which the conditions of Pareto optimality hold, Davenport was inclined to build an image under incomplete private property rights and substantial transactions costs. This fact has led some historians of economics to include Davenport among the American institutionalists.

Davenport's attempt to purge catallactics of value judgments was disregarded by the economics profession. The reason was the rise first of utilitarian welfare economics and later of "modern" welfare economics. A reassessment may be warranted today, however, particularly by economists with a new institutional bent.

In the field of what economists today call macroeconomics, Davenport made three significant contributions. By far the most important was his *theory of loan fund capital* – a theory of free enterprise in the supply of loan funds, including bank loans. In this theory, a person may try to issue money based on any kind of promise, although promises ordinarily are backed by some kind of material guaranty. This approach led to a theory of crises in which the main cause was errors in the appraisement of promises, errors that were exaggerated by excessive paper money creation. With the development of central banking, which began in the U.S. about the same time as his main book on the subject was published (1914), this ingenious (and in the author's opinion quite correct and insightful) theory was, in part, rendered irrelevant. The part that remained relevant was treated more fully by other writers on the credit system. Today, it is relevant only to those economists interested in free enterprise in banking. Davenport is also noted for one of the earliest treatments of the unemployment problem (Dorfman, 1949, 379-80) and as a contributor to the theory of fractional reserve banking (Humphrey, 1987; Marget, 1932).

Davenport, Herbert J. (1894) "The Formula of Sacrifice." *Journal of Political Economy*. 2 (September): 561-573.

Davenport, H. (1908) *Value and Distribution*. Chicago: University of Chicago Press.

Davenport, H. (1914) *Economics of Enterprise*. New York: Macmillan.
Frank Knight in the Encyc. if the S o d Sciences. article by

Dorfman, Joseph. (1949) "Herbert Joseph Davenport: Conflict of Loyalties." in Joseph Dorfman. *The Economic Mind in American Civilization: 1865-1918*. Volume 3: 375-390. New York: Viking.

Fisher, Irving. (1908) "Davenport's Value and Distribution." *Journal of Political Economy*. 16 (1): 661-679.

Gunning, J. Patrick. (1998) "Herbert J. Davenport's Transformation of the Austrian Theory of Value and Cost." In Malcolm Rutherford (ed.). *The Economic Mind in America: Essays in the History of American Economics*: London: Routledge.

Gunning, J. Patrick. (1998b) "H. J. Davenport's Loan Fund Theory of Capital." *Journal of the History of Economic Thought*. 20 (3): 349-369.

Homan, Paul T. (1931) "Herbert Joseph Davenport 1961-1981." *American Economic Review*. 21 (December): 696-700.

Humphrey, Thomas H. (1987) "The Theory of Multiple Expansion of Deposits: What It Is and Whence It Came." *Economic Review (Federal Reserve Bank of Richmond*). (March/April): 3-11.

Kendrick, M.S. () "Davenport, Herbert Joseph." *Dictionary of American Biographies: Vol 21*. New York: Shribner.

Marget, A. W. (1932) "The Relation Between the Velocity of Circulation of Money and the 'Velocity of Circulation of Goods' I."Journal of Political Economy. 40 (3): 289-313.

Newman, Philip C. (1952) "Herbert J. Davenport." In *The Development of Economic Thought*. (246-250) Englewood Cliffs, N.J., Prentice Hall.

Spiegel, Henry W. "Davenport, Herbert J." In Spiegel (ed.) (1952) *The Development of Economic Thought*. New York: John Wiley.