

The New Science of Economics in Mises's Treatise

Outline

1. The Classical Economists and the Liberal Ideology
2. The New Science of Economics
 - a. From Ideology to Science
 - b. Why Economics is Scientific
3. How Mises Presented the Science
 1. The Critics of Capitalism
 2. From Pure Praxeology to the Study of Action under the Conditions of Capitalism
 3. The Method of Imaginary Constructions
 - a. Imaginary Constructions and Reality
 4. [The Pure Market Economy](#)
 5. Economics
- B. Conclusion

Is economics a science? Yes, and Ludwig von Mises made it so. This essay shows how Mises transformed the liberal ideology of the classical economists into a science and how he presented that science in his treatise, *Human Action* (1966 – HA).

The essay is important for at least two reasons. First and foremost, the vast majority of writers of the Mises Institute have downplayed Mises's scientific economics and promoted the view that Mises based his writings on the utilitarianism of the classical economists.¹ As a corollary, they have promoted Murray Rothbard's anti-government, ethics. One who wants an accurate picture of Mises's economics must disregard such promotion. Second, modern professional economists are not familiar with this alternative. Yet, a strong argument can be made that almost all of the errors made by these economists over the years could have been avoided if they had studied and learned from Mises's works.

1. THE CLASSICAL ECONOMISTS AND THE LIBERAL IDEOLOGY

Economic science can be traced to the discoveries of the classical economists like David Hume, Adam Smith, and David Ricardo. They discovered the great principle that when human beings are free to trade and specialize and when they can own the material goods they acquire in trade, they

¹A good example is Walter Block. My published interchange with Block is [here](#).

have incentives to take advantage of the higher physical productivity of the division of labor (HA: 157-9), according to Ricardo's principle of comparative advantage (HA: 159-60).

The discoveries made by the classical economists became the basis for their writings and teachings. Since these teachings were at least partly accepted by the political leaders of the period, they also became the basis for the liberal international trade policies of the 19th century. They led many governments to adopt policies toward private property rights, free enterprise, money and fraud that promoted progress within a nation. In addition, they ushered in what is often referred to as the "Golden Age of International Trade," which lasted from the mid 19th century until World War I (Mises: 1927: xvi). The most energetic makers of the US constitution read this classical liberal *ideology* and incorporated it into their vision of the new nation.

Ideology is not the same as religion. The two are similar in that individuals use both to plan their actions. However, religion promotes a view about what the ends of an action should be. Proponents of the liberal ideology take it for granted that humans aim to achieve material ends. But they are silent about what the ends should be (HA: 155-7).

Many intellectuals and political leaders opposed the liberal ideology. Marxist, socialists, progressives and special-interest pressure groups recommended anti-liberal market interventions, protectionist policies, revolt, and militaristic nationalism. Nevertheless, the classical liberal principles have survived.

These principles also survived the catastrophic world wars of the first half of the twentieth century and depression of the 1930s. They became the foundation for the postwar General Agreement on Tariffs and Trade and the World Trade Organization. And they were the basis for what ultimately became the European Union. These organizations, and other organizations and international trade agreements, have continued the free trade tradition started by the classical economists. The liberal ideology also played a role in post-war U.S. trade policy, particularly toward the Asian dragon, Japan, and the Asian tigers of Taiwan and South Korea.

2. THE NEW SCIENCE OF ECONOMICS

The classical economists were pioneers. However, their knowledge was improved upon by what Mises called the modern subjective or modern value theory (HA: 3), which was advanced by Carl Menger, Eugen von Böhm Bawerk, J. B. Clark and others. The improved version states that the *conditions of capitalism* give individuals, acting in the entrepreneur role, incentives to produce material goods that tend to be in the best interest of individuals acting in the consumer role. The conditions of capitalism include private property rights, free enterprise, and control over fraud. Under these conditions, the entrepreneurs have a tendency to act in accord with the principle of [consumer sovereignty](#) (HA: 270-2).

From Ideology to Science

The liberal ideology is an ideology about government. It is not science. Like interventionism and socialism, it guides peoples' actions. It helped the political leaders and international traders bring peace and prosperity to their nations at least for the period during which classical economics was popular. These leaders knew nothing about the new science. Their policies were in broad accord with

the classical liberal ideology. The task of transforming this ideology into a science, while incorporating the ideas of the subjective value theorists, was left for Mises. He completed it with his publication of his treatise.

Why Economics is Scientific

The knowledge produced by the new economists is practical. It helps individuals attain their ends. Being practical, it fits into a larger class of knowledge that people have regarded as scientific. It is scientific in that it helps individuals attain their ends. It is not the use of the experimental method or the clever employment of statistical analysis of observed data that makes a type of knowledge scientific. It is scientific because human beings, considered as a group, believe that they can benefit from it. In this respect, it is analogous to the knowledge of produced by the natural scientists.

Objections that have been made against this point of view are associated with the terms “scientism” and “positivism.” In his last book on economics, Mises soundly refuted positivism in economics. I describe this refutation [here](#).

3. HOW MISES PRESENTED THE SCIENCE

It is difficult to read Mises’s introduction to his treatise without forming the opinion that the primary reason for presenting the new science the way he did was to deal with critics. While this is not the only purpose, the reader will benefit if I start by identifying these critics. It will help him realize the significance of Mises’s decision to start with praxeology.

The Critics of Capitalism

It is convenient to divide the critics of capitalism into three groups. The first two were critics of the classical economists: utopian socialists and Marxian polylogists. The utopians asserted that socialism is a better system of organization than capitalism. These critics not only failed to appreciate the teachings of the classical economists, they did not seriously explore the implications of the system they proposed to replace it. Mises dealt with these critics in his 1922 book, *Socialism: An Economic and Sociological Analysis* (1922).

The most vociferous critics of classical economics were Karl Marx and his followers. Marx denied that the “laboring class” could be helped by classical economics. The reasoning of classical economics could only help the “capitalist class” but not the “laboring class.” This denial prompted Mises to call Marx’s idea “polylogism.” This is the proposition that there is more than one way to reason. One who subscribes to polylogism denies the possibility of a single logical structure of the human mind. This enables her to deny

Polylogism: the proposition that there is more than one means of reasoning and, therefore, that there is always potential disagreement upon whether a particular means is more apt to achieve an end. Alternatively, it is the proposition that there is no single logical structure of the human mind.

that economics is a universal science of the means.² In the absence of a single mode of reasoning, a person who uses logic to persuade others that a particular means is unsuitable for attaining an end could succeed only if the target of her persuasion possesses the same structure of mind as she possesses. She could not persuade a targeted individual who possesses a different structure. For instance, a “capitalist class economist” could not employ logic to persuade a “laboring class economist.”

A third set of critics asserts that science must be defined by its methods of study. One subset of members of this class are the historicists who falsely believed that history can be studied without theory. Menger had effectively refuted the historicists of the 19th century. Newer members of this class were the “panphysicalists,” the “positivists” and the “behaviorists.” These maintained that to be a scientist, an economist would have to use the methods of the natural sciences. What these groups have in common is the implicit assumption that the events of the past are repeatable.

To refute all of the critics who assumed that the events of the past are repeatable, Mises sought to build the “system of economic thought” in such a way that it is “proof against any criticism on the part of irrationalism, historicism, panphysicalism, behaviorism, and all varieties of polylogism” (HA: 7). Thus, he set out to “build the theory of catallactics [economic theory] upon the solid foundation of a general theory of human action, praxeology” (*ibid.*). In accord with this aim, he began his presentation with praxeology.

From Pure Praxeology to the Study of Action under the Conditions of Capitalism

Mises’s starting point was to develop praxeology – the theory of action in general, or action as a category. To do this he first identified the [prerequisites of action](#) in his chapter 1. He then digressed in chapters 2 and 3 to discuss the various classes of criticisms that I cited above (*ibid.*). Chapters 4, 5 and 6 returned to praxeology in order to derive the [necessary characteristics of action](#). With one exception, he designed the

Praxeology: the study of action in general, or action as a category. It consists of producing concepts and theorems that are derived exclusively from the general category, or concept, of distinctly human action.

subsequent seven chapters, up to chapter 13, to bridge the gap between action in general and interaction under the conditions of capitalism – market interaction, which is the subject matter of economics (HA: 233). One might say that he sought in these early chapters to build a vocabulary for economics that is rooted in praxeology. In his chapter 7, he writes about applying labor in the production of material goods for the purpose of exchange. His chapter 8 describes the division of labor law. His chapter 10 introduces decision-making in an image of interaction that contains money prices (calculative action or action that entails monetary calculation). His chapter 11 introduces the images of direct and indirect exchange. His chapter 12 highlights the study of interaction under pure capitalism by introducing a “sphere of economic calculation, or sphere of capitalism. His chapter 13 expands on the distinction between action under the conditions of capitalism and other action. It elaborates on the meaning of monetary calculation as a means of decision making. And it elaborates on economic calculation as a characteristic of interaction under the conditions of capitalism. Thus,

²Indeed, a consistent polylogist must deny the possibility of a universal natural science as well.

he gradually shifted from the study of the action character of human beings to the study of interaction under the conditions of pure capitalism.

The Method of Imaginary Constructions

Mises began his elucidation of the subject of economics in his chapter 14 on the scope and method of economics. Almost immediately, he writes that the method of economic science is the method of imaginary constructions. He writes that this is also the method of praxeology.³ He does not present an argument to support his statement. He merely gives examples of imaginary constructions, telling the reader more or less how these constructions are used. Nevertheless, he does provide a recipe:

The main formula for designing of imaginary constructions is to abstract from the operation of some conditions present in actual action. Then we are in a position to grasp the hypothetical consequences of the absence of these conditions and to conceive the effects of their existence. Thus we conceive the category of action by constructing the image of a state in which there is no action, either because the individual is fully contented and does not feel any uneasiness or because he does not know any procedure from which an improvement in his well-being (state of satisfaction) could be expected. Thus we conceive the notion of originary interest from an imaginary construction in which no distinction is made between satisfactions in periods of time equal in length but unequal with regard to their distance from the instant of action (HA: 237).

Unfortunately, the examples are not easy for the reader to fathom. His first example of the category of action refers to the derivation of the prerequisites and necessary characteristics of action. In other words, Mises is referring to his work in his chapters 1, 4, 5 and 6, where he used the counterfactual to produce vocabulary to refer to the category of action. However, he does not actually say this and his derivations in those chapters did not use the term “imaginary construction.” His second example is of “originary interest.” This example is difficult to fathom, partly because he attaches more than one meaning to this term, as I point out in my essay “[How to Build Economic Theory](#).” As a result, the typical reader is unlikely to be informed by this recipe.

Imaginary Constructions and Reality

It has sometimes been argued that because imaginary constructions are not derived from realistic assumptions, they cannot be helpful. Such an argument certainly does not apply to pure praxeology. The counterfactual imaginary constructs are not real. But the prerequisites and necessary characteristics are real to every person who is in a position to bethink and reflect. Recognizing this, Mises writes:

The imaginary constructions of praxeology can never be confronted with any experience of things external and can never be appraised from the point of view of such experience. Their function is to serve man in a scrutiny which cannot rely upon his senses (HA: 237).

It does not apply to economics either, as Mises argues in his chapter 11, in which he explains his use of the image of direct exchange.

³HA: 36.

The Pure Market Economy

The specific conditions of capitalism may vary. Accordingly, as pointed out in Part One, the economist begins his study of market interaction with the imaginary construction of pure capitalism (the pure market economy). Thus Mises writes:

The imaginary construction of a pure or unhampered market economy assumes that there is division of labor and private ownership (control) of the means of production and that consequently there is market exchange of goods and services. It assumes that...the government, the social apparatus of compulsion and coercion, is intent upon preserving the operation of the market system, abstains from hindering its functioning, and protects it against encroachments on the part of other people. The market is free; there is no interference of factors, foreign to the market, with prices, wage rates, and interest rates. Starting from these assumptions economics tries to elucidate the operation of a pure market economy (HA: 237-8).

The economist can never build an image of all of the interaction under pure capitalism (i.e., the pure market economy). This is one reason that he calls the pure market economy an imaginary construction. Market interaction is the consequence of numerous, often uncountable, individual decisions. Each decision is a contributing factor. And many of the decisions are intertwined. Some people make decisions by trying to anticipate the decisions of other people. To build a complete image, he would have to identify every decision and the complex thought processes that preceded it.

Recognizing humankind's inability to represent all decisions, the economist builds an image of interaction by producing a set of *ceteris paribus* theorems. The theorems show how distinctly human actors would take advantage of the higher physical productivity of the division of labor while, at the same time, dealing with the scarcity of means of production. The method of producing economic theorems and of building an image of the pure market economy is discussed at length in my essay "[How to Build Economic Theory.](#)"

Economics

To present economics means to present the economic theorems. Beginning with his chapter 15, Mises went on for nine chapters to develop additional constructs and theorems for the pure market economy. His entire Part Four of HA – the part he labeled “Catallactics or Economics of the Market Society” – is devoted to the production of theorems for this imaginary economy. The part covers chapter 15-24.

Part 5 of HA consists of two chapters in which Mises uses the theorems he had produced in his part 4 as a basis for building additional theorems to evaluate the claims made by socialists. He defines socialism as a social system that its proponents tout as a means of taking advantage of the higher physical productivity of the division of labor without establishing the conditions of capitalism. He shows that such an aim is impossible to achieve due to the absence of private property rights and accurate entrepreneurial calculation. By these means, he shows that the ideology of socialism is a false ideology.

In part 6, he tackles market intervention. In doing so, he fulfills the implicit promise he had made earlier in his chapter 14 on scope and method. He had written that the economist begins by elucidating the imaginary construction of the pure market economy. Then,

at a later stage, having exhausted everything which can be learned from the study of this imaginary construction, [he turns] to the study of the various problems raised by interference with the market on the part of governments and other agencies employing coercion and compulsion (HA: 238).⁴

He spends all of part six – a total of ten chapters – evaluating arguments in favor of market intervention. He concludes HA with three chapters that are of no concern here.

4. CONCLUSION

Anyone who regards knowledge of how to satisfy wants for material consumer goods as useful or practical cannot help but admit that the knowledge upon which the classical economists based their liberal ideology is scientific in the same sense that knowledge of the benefits of crop rotation, of fossil fuels as energy sources, of stem cell transplants as a potential cure for cancer is science. Nevertheless, no one today realizes that Mises produced this new science of the means. No one realizes that Mises was able to link (1) the fundamental premises of the liberal ideology to (2) the satisfaction of wants for material consumer goods.

All knowledge is not science. Some knowledge does not help human beings produce more material consumer goods than otherwise. Moreover, some knowledge that does help in the production of more material consumer goods is not produced for that purpose. It is not motivated by a desire to achieve this aim. Nevertheless, if one takes the capacity to produce greater amounts of material consumer goods as the defining characteristic of science – as the characteristic of knowledge that must be present if that knowledge is to be called “science” – there is no doubt that Mises was the first to produce economic science.

You can find more on Mises’s scientific economics [here](#).

[Other Austrian Economics Commentary](#)

Please send feedback:

Email: gunning@nomadpress.com

[Go to Pat Gunning's Pages](#)

⁴Mises does not immediately say what he means by “various problems raised by interference.” A careful reader can easily find out two paragraphs later. He writes that “a careful unbiased scrutiny of all aspects of interventionism” yields

the conclusion that the goals which most people, practically even all people, are intent on attaining by toiling and working and by economic policy can best be realized where the free market system is not impeded by government decrees (*ibid.*).

References

Mises, Ludwig von. (1951 [1922]). *Socialism: An Economic and Sociological Analysis*. New Haven: Yale University Press.

Mises, Ludwig von. (1978 [1927]). *Liberalism*. Kansas City: Sheed, Andrews and McMeel.

Mises, Ludwig von. (1966) *Human Action: A Treatise on Economics*. Chicago: Henry Regnery Company. Originally published in German in 1940.

Mises, Ludwig von. (1978) *The Ultimate Foundation of Economic Science: An Essay on Method*. Kansas City: Sheed, Andrews and McMeel. Originally published in 1962 by Van Nostrand, Princeton, N.J.