Unintended Consequences: The Austrian Approach to Social Phenomena

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A Personal Remark

John M. Virgo, † 29 November, 2012
Plan of the Address

1. Dramatis personae: The Austrian School of Economics
2. Carl Menger
3. What are unintended consequences?
4. Example ("case study"): Menger on the origin of money
5. Why this may be of interest today
Who are the Austrians?

• The Founding Father: Carl Menger
• 2\textsuperscript{nd} generation: Eugen von Böhm-Bawerk, Friedrich von Wieser, ...
• 3\textsuperscript{rd} generation: Ludwig von Mises, ..., Joseph A. Schumpeter
• 4\textsuperscript{th} generation: Friedrich A. von Hayek, Gottfried Haberler, Oskar Morgenstern, Fritz Machlup, ...
• Contemporary Austrians: mostly not in Austria
A Gallery of Austrian Economists

Carl Menger (1840-1921)
Carl Menger (1840-1921)
Eugen von Böhm-Bawerk (1851-1914)
Friedrich von Wieser (1851-1926)
Ludwig von Mises (1881-1973)
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Joseph Alois Schumpeter (1883-1950)
Friedrich August von Hayek (1899-1992)
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Friedrich August von Hayek (1899-1992)
Oskar Morgenstern (1902-1977)
John von Neumann with Oskar Morgenstern
Oskar Morgenstern (1902-1977)
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Contemporary Austrian Economics

• Migration of the tradition (K. Vaughn): emigration in the 1930s (®A. Hitler)

• Flowering in the USA:
  • Scientific work: Mises, Hayek, M. Rothbard, L. Yeager, I. Kirzner, D. Lavoie, P. Boettke, L. White, M.J. Rizzo, S. Horwitz, E. Stringham,...
  • Political influence: libertarianism; Liberty Fund, Mises Institute; R. Paul, Tea Party movement,...

• Outside the USA: e.g. L. Lachmann, L. Robbins
Carl Menger

- Born 1840 Neu-Sandec (Nowy Sacz)
- Studied law and economics in Prague and Vienna
- PhD Cracow
- 1871 *Grundsätze der Volkswirtschaftslehre* (Principles of Economics; tr. 1950), “1st part“; 2nd ed. by son Karl 1923
- 1873 Associate Professor, University of Vienna
- 1879 Full Professor, University of Vienna
Carl Menger

- 1876 – 1878 Lecturer to Crown Prince Rudolf
- 1883 Untersuchungen über die Methode der Socialwissenschaften und der Politischen Oekonomie insbesondere (Problems of Economics and Sociology; Investigations into the Methods of the Social Sciences; tr. 1963)
- First Methodenstreit (methodological debate, against Gustav Schmoller)
Carl Menger

- **Influence** in:
  - Italy: M. Pantaleoni, L. Cossa, A. Graziani,…
  - Holland: N. Pierson
  - USA: S.N. Patten, R. Ely
  - France, other parts of Habsburg monarchy,…
- Work on capital theory, money (On the Origin of Money, *EJ* 1892), currency reform
- Hofrat, member of the Herrenhaus (House of Lords)
- Retired 1903
- Died 1921
Menger and the Neoclassical School

- Menger as a father of neoclassical economics (together with Jevons and Walras):
  - Methodological individualism
  - Homo oeconomicus
  - Subjective theory of value
  - Marginalism
  - Price theory: monopoly, (perfect) competition
  - Money: double coincidence of wants
- But non-neoclassical elements in his theories:
  - Dynamics vs. equilibrium
  - Supply and cost not elaborated (Wieser: opportunity cost)
  - Mathematics of limited use in economics – methodology
- Incorporation into neoclassical mainstream (until 1930s)
Menger’s Subjective Value Theory

Individual

Needs

Constraints

Value

1st order goods

2nd order good 1

2nd order good 2

...  

2nd order good n

Value
Unintended Consequences

• Predecessor: **Adam Smith** 1776

  “By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. [...] By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it.”
Unintended Consequences

• Robert K. Merton, The Unanticipated Consequences of Purposive Social Action, ASR 1936:

“[...] the consequences of purposive action are limited to those elements in the resulting situation which are exclusively the outcome of the action, i.e., those elements which would not have occurred had the action not taken place. [...] These sum-total or concrete consequences may be differentiated into (a) consequences to the actor(s), (b) consequences to other persons mediated through (1) the social structure, (2), the culture and (3) the civilization.“
Unintended Consequences

• Raymond Boudon, *The Unintended Consequences of Human Action*, 1982:

  “The number of possible recombinations of the following criteria does, therefore, define the number of possible configurations: 1. No participant (1a), some participants (1b), all participants (1c) attain their individual objectives; 2. Producing, at the same time, benefits (2a), or problems (2b), or else collective benefits and problems (2c); 3. Each of these applying only to some (3a), or to all the participants (3b).“
Unintended Consequences

  1. Social (collective) consequences
  2. Not intended by any individual
  3. Mediated through many individuals
  4. Individual intentions directed at individual level
  5. Action of one individual not sufficient
  6. No collective intentionality
Menger‘s Problem

• Pragmatic vs. organic phenomena: results of common will (design) vs. unintended results of human efforts aimed at attaining individual goals
• Against superficial analogies natural – social sciences
• Against organicism and holistic explanations – in favor of exact = atomistic understanding in social sciences
• Against German Historical School
Menger’s Problem

“[...] we meet a noteworthy, perhaps the most noteworthy, problem of the social sciences: How can it be that institutions which serve the common welfare and are extremely significant for its development come into being without a common will directed toward establishing them?”

Examples of such social institutions: money, settlements, the state, language, law, morals, markets and “numerous institutions of economy”
Menger on the Origin of Money

- Barter economy
- Some goods are gradually accepted by everyone
- Also by those who have no need for them
- Only in some cases money introduced by agreement or legislation
- Difficulty of double coincidence of wants
- Individual interest: obtain marketable goods
- Most marketable goods start to be accepted by most successful individuals
- Propagation through imitation, “practice and custom”
- Money unplanned outcome of individual efforts
Why can this be of interest today?

• Central tenet of later and contemporaneous Austrian Economics: Hayek’s spontaneous order, Socialism Debate,...


• Influence of methodology on other social sciences, e.g. sociology – “economic imperialism”
THANK YOU FOR YOUR ATTENTION!