

COLLECTED WORKS OF CARL MENGER

Since 1930, when the first of its Reprints of Scarce Tracts in Economic and Political Science appeared, the London School of Economics has made one important contribution after another to filling in the gaps in contemporary economics libraries. The works selected by the editors for reprinting have not only been of outstanding importance in the history of economic thought, but have also been specially welcome because of their inaccessibility to the majority of students in the field. Menger's collected works, the latest addition to the series, rank high in both respects. Menger's importance in the history of economic thought is too well recognized to require special comment. As to the inaccessibility of his works, the present writer can testify from personal experience that even in Vienna the first edition of the *Grundsätze* and the two books on methodology¹ are the greatest of rarities. Professor Hayek appears fully justified in attributing to this scarcity the fact that theories originally developed by Menger himself are known to the world chiefly through the writings of his disciples Bohm-Bawerk and Wieser.² Economists are bound to feel genuinely grateful to the London School for meeting so real a need.

I

To Menger, more than to any other single writer, belongs the credit — and the responsibility — for the subjective value departure in economics. The appearance of his works in a form which, for the first time in fifty years, makes possible their widespread distribution furnishes a good occasion for a review of what that departure has meant. Such a review can

1. *Untersuchungen u.d. Methode der Sozialwissenschaften und der Politischen Oekonomie insbesondere and Irrtümer des Historismus.*

2. Introduction to the Collected Works, I, xxv. Menger's *Grundsätze* had already been out of print for some time by the nineties. He refused, however, to allow a reprint, in the expectation — unrealized in his lifetime — of bringing out a second, completely revised edition.

furthermore be undertaken today with a much better prospect of attaining both clarity and agreement than at any previous time in the last half century.

Subjective value theory has, since its inception, been one of the major storm centers of economics. Proponents have made extravagant and dogmatic claims as to its importance, while opponents, sensing something wrong and yet failing to put their fingers on the precise spot, have denounced the whole subjective analysis as a tangle of verbal duplications and terminological ambiguities. Careful analysis of the problems involved shows that there should be little cause for surprise at this situation. Many of the concepts involved are slippery in the extreme, and distinctions which are essential to clarity are easily overlooked.

That the prospect for mutual understanding has greatly improved in the last few years is attributable basically to the advances that have been made in the general field of scientific methodology, the effects of which are now being felt in the social sciences. A number of the post-war generation of sociologists and economists have, in particular, been doing excellent work in recent years in applying the lessons of modern scientific criticism to the problems of their own special fields. As examples of this development such widely separated and diverse writers as Professor Gunnar Myrdal of Stockholm, Dr. Ralph W. Souter, formerly of Columbia, and Dr. Felix Kaufmann of Vienna, may be mentioned.³

The last named scholar is particularly important for purposes of the present discussion. For one thing, his recently published *Methodenlehre der Sozialwissenschaften* offers

3. Myrdal: *Das politische Element in der Nationalökonomischen Doktrinbildung*. Berlin. 1932.
 "Das Zweck-Mittel Denken in der Nationalökonomie," *Zeitschrift für Nationalökonomie*, vol. 4.
- Souter: *Prolegomena to a Relativity Economics*. New York. 1933.
- Kaufmann: *Methodenlehre der Sozialwissenschaften*. Vienna. 1936. "On the Subject-Matter and Method of Economic Science," *Economica*, vol. 13.
 "The Concept of Law in Economic Science," *Review of Economic Studies*, Feb. 1934.

probably the most comprehensive survey of the methodological problems of the social sciences as yet undertaken in the light of modern logical and scientific advances. In addition to this Dr. Kaufmann is an Austrian who grew up in close personal contact with the members of the Austrian school of economists. His analysis of utility theory is consequently developed with an intimate and sympathetic understanding of what the utility theorists were trying to do.

In what follows I do not propose to undertake anything like a general survey of Menger's works. Within the limits of economic theory, Menger applied himself to a considerable diversity of problems, each one of which he handled with characteristic firmness and originality.⁴ But all these parts of his work are of secondary importance compared with his introduction of the subjective value approach into economics. It is accordingly with the latter and the problems arising out of it that the following discussion will be concerned.

II

We may start with a summary of the major assumptions involved in the subjective value approach to the problems of economics: (1) prices (or exchange values) can best be explained by reference to the choice acts of individual consumers; (2) consumers by and large act in accordance with coherently formulated plans, and hence prediction as to what they will do is possible, at least in principle;⁵ (3) certain general features of the internal structure of consumers' plans are sufficiently obvious to provide the basis for a skeleton

4. Most important are his treatment of capital theory, his contributions to the theory of money, and his remarks on the problem of imputation (*Grundsätze*, pp. 138-142). All of these are discussed in Professor Hayek's introduction to the *Collected Works*.

5. This is the assumption of rational conduct, i.e., conduct in accordance with a plan, which will be discussed in more detail below. It is interesting to compare Max Weber's often cited formulation of this assumption: "Marginal utility theory, for its own particular purposes, treats human conduct as though it ran from A to Z under the control of commercial calculation; i.e., calculation based on the knowledge of all relevant conditions." *Gesammelte Aufsätze zur Wissenschaftslehre*, p. 370.

theory of price formation; (4) detailed study of consumer habits may well yield information about the way certain groups or classes of consumers are likely to react in various concrete situations and thus to prove useful for such purposes as, for instance, predicting how the demand for a certain commodity will change with changes in its price or in its buyers' incomes.

It will be convenient to leave the first assumption for later consideration and to begin with an analysis of the second. The meaning of conduct in accordance with a plan is formulated for the purposes of subjective value theory in the marginal utility principle. Put in the most neutral way possible, the marginal utility principle relates the relative importance attached to different goods by the individual consumer to the relative importance of possible uses for the goods, which the consumer already has worked out in his head.⁶ The uses, with their relative importance, constitute a system of ends the means to the attainment of which are the available goods. In so far as he acts rationally, the consumer will estimate the relative importance to himself of any unit of a good by the relative importance of the use he would have to sacrifice if he were to lose the unit in question. He will, furthermore, prefer any unit of a good to any other unit of the same or a different good if the importance he attaches to the use that would have to be sacrificed without the first unit is greater than that attached to the use that is dependent on the second unit.

Now the important thing to be noted here is that the marginal utility principle as stated can be interpreted in two quite different ways, failure to distinguish between which has proved a source of endless confusion. Looked at in one way, it is merely a *definition* of rational conduct. What the theorist is in effect saying is: "When I speak of rational evaluation of goods on the part of a consumer, I shall mean

6. The basis for the individual's decisions, i.e., whether in response to physiological need, aesthetic taste, or what not, as to which uses are more and which are less important is not an essential part of the utility principle itself. Cf. the discussion of needs below.

evaluation in accordance with a hierarchy of uses which is characterized by such and such internal relationships.”⁷ Since the marginal utility principle, so regarded, merely defines rational conduct there can be no question of its verification in practice. In fact it may be entirely unrelated to anything in reality, since our ability to conceive of action in accordance with an internally consistent plan is quite independent of the way people actually do act.

But the marginal utility principle may also be intended as a hypothetical assertion of fact. Its meaning in this case is: “If people act rationally, then they will, as a general thing, estimate the relative importance of different goods in accordance with a scale of uses which exhibits such and such characteristics,” the necessary implication being that it is possible to determine independently of the specific acts predicted whether or not they are acting rationally. The accuracy of the prediction is then subject, in any case or group of cases where it is applied, to the test of empirical verification.

The failure to distinguish between these two interpretations is, partly at least, attributable to the fact that the definition is frequently stated in the same form as the assertion of fact. That is, the sentence: “If a man acts rationally, he will do so and so” may be interpreted in either way.⁸ Beneath the verbal ambiguity, however, is the more fundamental failure to draw a sharp distinction between purely logical deductions, that is, the working out of implications

7. The specification of this internal structure of the system of ends may be more or less complete according to the purpose the theorist has in mind in constructing his concept. Cf. Kaufmann, *Methodenlehre*, p. 261.

8. At the risk of elaborating the obvious, this point may be restated as follows: Is it possible for a rational being to act otherwise than in accordance with the marginal utility principle? If the marginal utility principle is viewed merely as a definition of rational conduct then it clearly is not, since we are agreeing to call only that conduct rational which exhibits the characteristics specified in the marginal utility principle. If, however, what we mean to say in stating the marginal utility principle is that we think rational people *as a general thing* do and will act in the specified manner, then we of course have to admit the possibility of exceptions and it is perfectly conceivable that a rational being — however identified — would not act in accordance with the marginal utility principle.

already "contained in" the initial concept or system of concepts, and empirical laws, which are predictions as to the course of events in the real world.

The failure to observe this distinction, which has been widespread among economists, comes out with particular force in the methodological controversy between Menger and the German Historical School, led by Schmoller. Menger based his whole argument on what he conceived to be a fundamental distinction between mere "empirical laws," i.e., "observed regularities in the sequence and coexistence of economic phenomena"⁹ and exact theoretical laws, which, arrived at by the process of abstraction, reduce the complicated phenomena of reality to their "simplest, rigidly typical elements."¹

This notion that in economics there are two kinds of laws — "mere" empirical generalizations and "exact" theoretical laws — both of which in some obscure way are applicable to reality, has persisted down to the present time. Recent examples may be found, for instance, in the writings of Professor Robbins and Professor Hayek.²

In his recently published essay on "Collectivist Economic Planning" Professor Hayek states categorically that since experiment in the social sciences is "impossible" we can have "no knowledge of definite regularities in the complex phenomena in the same sense as we have in the natural sciences." There is, however, a different sense in which the social sciences can know about the phenomena they are interested in. Professor Hayek explains the difference as follows: "There

9. *Irrtümer des Historismus*, p. 18.

1. Altho the Germans lacked the critical tools necessary to work out their position in a thoroly satisfactory way, it seems to me that they were guided by the sounder instinct of the two. Cf., for instance, Schmoller's warning that starting from hypotheses only hypothetical assertions can be made, "to which one should not attempt, through the use of the misleading word 'exact,' to give a false appearance of scientific rigor (den Schein der strengsten Wissenschaftlichkeit)." *Jahrbuch für Gesetzgebung*, 1883, p. 243.

2. Robbins, *The Nature and Significance of Economic Science*, London, 1932. Hayek, *Collectivist Economic Planning*, London, 1935.

can be no doubt the social as well as natural sciences have to employ deductive reasoning. The essential difference is that in the natural sciences the process of deduction has to start from some *hypothesis* which is the result of *inductive generalizations*, while in the social sciences it starts from *known empirical elements* and uses them to find the regularities in the complex phenomena which direct observation cannot establish." (Italics mine.) It is too bad that Professor Hayek does not enlighten us further as to the nature of the "known empirical elements" which so conveniently absolve the social sciences from the necessity of making "inductive generalizations." In the absence of such enlightenment it is impossible to determine more exactly the root of this peculiar concept of law as applied to the social sciences.

A related misunderstanding, tho in its origin apparently not identical, has been pointed out by Mr. T. W. Hutchison,³ in Professor Robbins' *Nature and Significance of Economic Science*: "In a recent pronouncement on these problems, the following occurs: 'It is this inevitability of economic analysis which gives it its very considerable prognostic value. It has been emphasized sufficiently already that Economic Science knows no way of predicting what will be the given data at any particular point of time. . . . But given the data in a particular situation it can draw inevitable conclusions as to their implications.' A contradiction appears at once, and a failure to distinguish between implication and inference may be at the bottom of it. This distinction may be summed up by saying that implications take the form 'if p, then q,' and inferences the form 'since p, therefore q.' The one shows formal connections, the other states conclusions about the real world. An inevitable implication is a tautology, and can no more prognosticate anything than can the multiplication table. An inference, on the other hand, requires some data to be known in order to establish a 'since.' But the foregoing quotation says that 'Economic Science knows no way of predicting what will be the given data at any particular point of

3. "A Note on Tautologies," *The Review of Economic Studies*, February, 1935.

time.' It follows, if this is to be taken *au pied de la lettre*, that Economic Science can predict nothing."

III

To this logical confusion must be added as a further source of misunderstanding the elusive nature of the "facts" with which utility theory deals. We have just seen that in its attempt to explain exchange relationships utility theory goes back to a scale of valuations which is supposed to exist in the head of the consumer prior to his coming into the market. On the basis of what is "known" about this scale of valuations certain predictions are, in principle at least, possible as to what the person in question will do. But the separation of the known from the unknown in dealing with such psychological data as subjective scales of valuation is an extremely slippery job. It is little wonder that most utility theorists have fallen into the logical error of inferring the consumer's scale of valuations from his actual behavior in the market, while at the same time pretending to explain the behavior on the basis of the preëxisting valuations.

In the case of writers like Professor Mises,⁴ who specifically exclude any attempt to utilize psychological or biological data, the circularity of reasoning involved may be so obvious as to be harmless. But it is almost sure to be misleading in the case of utility theorists who, like Menger himself, take as their starting point a study of concrete needs and wants.⁵ The purpose of such a study is to discover in the relative intensity of the different needs a clue as to the relative importance of the different uses for goods. Now the danger here lies precisely in the fact that to a limited extent it is possible to make significant statements about the order of intensity

4. Mises, *Grundprobleme der Nationalökonomie*, Vienna, 1933. "People forgot that we can only know the need from the behavior, and that consequently the concept of behavior which does not correspond to the needs is nonsensical." P. 140.

5. "The theory of needs is of fundamental importance for economics, and at the same time the bridge which leads from the natural sciences, especially biology, to the social sciences." *Grundsätze der Volkswirtschaftslehre* (2d ed.), p. 1.

of at least the simpler human needs and desires.⁶ Examples of this can be found in the writings of all the earlier utility theorists who were forever indulging in long discussions of the relative intensity of the needs of a typical person for various amounts of drink, food, clothing, shelter and the like.

Had they been willing to confine themselves to this limited sphere no criticism could be made of their work. They were, however, looking for completely "general" and absolutely "exact" laws and as a consequence made the fatal mistake of so broadening the concept of need as to take in every motive or impulse to action of whatever sort. Any act of choice on the consumer's part came to be regarded as based on an estimation of the relative intensity of competing needs, the more intense need *always* winning out over the less intense. The proposed explanation of choices on the basis of a weighing of actually distinguishable needs — both the needs and the weighing being regarded as independent of the ensuing choices — thus ended up in a mere duplication of terms.

This misconception has been particularly unfortunate since it has greatly impeded progress in the realistic study of needs and need-complexes. Such positive results as have been achieved, as, for instance, in the analysis of complementarity, periodicity, and divisibility,⁷ have been incidental to the

6. Cf. Kaufmann, *op. cit.*, pp. 265-266: "Of two needs, that one is frequently characterized as the weaker or less important whose satisfaction is actually given up. In this way it appears that the choice acts are explained by psychological determinants, while in reality a new label for the decision expressed in the choice act has simply been introduced by way of definition. This misunderstanding is especially dangerous here, since in certain subsections of the territory under investigation such scales of intensity actually can be established. This is particularly true of such 'primitive' needs as those for food, drink, and clothing. Since, furthermore, the typical conditions of intensification or weakening of these needs are known, intensity-patterns (*Dringlichkeitstypen*) can be constructed, which may be useful for the explanation of economic behavior."

7. In this respect Menger deserves high rank among utility theorists. It is also worthy of note that most of the subsequent work of this sort has been done by his successors in Vienna, notably Professor Hans Mayer and Dr. P. N. Rosenstein-Rodan.

illusory search for an absolutely general and universally valid law of human behavior.⁸

With the discussion of needs and their place in subjective value theory we have covered the last three of the four major assumptions involved in the subjective value approach. There remain a few comments to be made on the first; that is, the assumption that the explanation of prices should start from the individual consumer.

The shift in emphasis from producer to consumer in the writings of the earlier marginal utility theorists was all to the good so far as it served merely to correct the classical economist's one-sided neglect of demand and to provide economists with a method of analyzing the factors that lie behind market behavior on the consumers' side. Other consequences of the shift in point of view have not been so beneficial. For one thing, it came, ironically enough, just at the turning of the high tide of free competition and the beginning of the modern development of monopolistic forms of market control. The new approach was thus from its inception a generation or more too late, the individual consumer obviously being a more appropriate focal point for the study of a freely competitive economy than for that of a partially trustified one.

Emphasis on the consumer also led easily, if not quite legitimately, to the construction of a picture of the whole of economic activity as directed toward the satisfaction of consumers' wants. Here again it is scarcely necessary to argue that this picture has been steadily losing whatever justification it may once have had. And finally the centering of

8. Offhand it seems somewhat paradoxical that the most serious attempts to make concrete use of consumer needs in economic analysis have come from writers like Loeb, *Chart of Plenty*, and Ezekiel, *\$2,500 a Year*, whose technocratic or institutional background would lead one to expect a complete repudiation on their part of anything so closely resembling a "utility" approach. Most avowed disciples of the marginal utility school, on the other hand, would roundly condemn the procedure followed in the studies just mentioned. All of which leads one to suspect that the bitter controversies between utility theorists and institutionalists really had very little to do with the apparent question at issue; namely, whether or not needs and desires might profitably be utilized in the attempt to explain economic phenomena.

attention on the individual consumer⁹ has led to a serious neglect of the various types of collective consumption, that is, consumption in the planning of which the individual participates as a "voter" and not directly as a buyer.¹

IV

Menger's contribution to the theory of value was unquestionably pioneer work of the highest order. With one brilliant stroke he cleared away the perplexity and confusion that had hitherto prevailed as to the rôle of subjective estimations of utility in the determination of value. One has to read over again some of the passages in which the older economists struggled with the apparent paradox of utility to appreciate fully the quality of Menger's achievement in this respect. The development of economic analysis was furthered in two important ways. In the first place, many sterile controversies and pseudo-problems were forever laid to rest, and in the second, a new and potentially fruitful line of inquiry was opened up.

But Menger and his disciples overreached themselves in attempting to universalize the significance of their discovery. Instead of being content to view the new subjective analysis as a corrective, on the one hand, for the one-sidedness of the older cost of production theories and as suggestive, on the other, of the way consumers of various types would act under

9. It is obvious, of course, that individual purchase and sale is neither the only, nor necessarily the best way — best, that is, from their own individual points of view — consumers can seek to satisfy their wants. Many highly important types of consumption are collective by their very nature and require the exercise of a collective decision as to whether they shall be enjoyed or not. Other types could be left to individual decisions — as for instance, the choice of architectural designs for city houses — but are of such nature that every one will be better pleased with the final result if a measure of collective restraint is placed on the individual decisions. The same applies to various forms of competitive consumption: every one concerned would frequently be happier if a collective agreement "to call it off" could be reached. These considerations, while commonplace enough, have usually been overlooked in discussions of "maximum consumer satisfaction."

1. Of course none of these defects is inherent in the marginal utility principle itself. They are rather a consequence of the lack of discrimination with which it has been used.

various circumstances, they professed to have discovered a universally valid law of human behavior. This led, as already pointed out, to a broadening of the concepts of need and want until they lost all their original common-sense content. It also led to Menger's misguided excursion into the field of scientific methodology: an excursion that was bound to end disastrously because of the logically contradictory nature of the goal it sought to reach.

In the recent revival of interest in Menger and the other earlier Austrian economists, attention has been concentrated on the supposed universal validity of the "laws" of subjective value theory. The chief fruits have been more bad methodology, combined with a neglect of much that was sound and potentially useful in Menger's treatment of the subject. His fresh and vigorous, if somewhat naïve, interest in concrete needs² and their interrelations has been deemed unworthy of the dignity and authority of economic science by his modern disciples. For Menger himself, however, the interest was a profound and continuing one. It is thus quite legitimate to consider present and future experimenters with consumption data — whether obtained from budget studies, the psychological or physiological laboratory, or observation of the experimenter's self and his acquaintances — as carrying on a line of inquiry in which Menger was one of the earliest pioneers.

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2. His effort to link utility theory to biology and physiology should be recalled.