BARRON'S ON BOOKS

From Realistic Theory Comes Sensible Advice

The Foundations of Modern Austrian Economics, edited with an introduction by Edwin G. Dolan. 238 pages. $12 hardcover, $4.95 soft. Sheed Andrews & McMeel, 6700 Squibb Road, Mission, Kan.

ONE of the most intriguing episodes in the history of economic theory concerns the Austrian school of economics. At the turn of the century, Austrian economists were amicably debating the English and French schools, and were bitterly disputing German Socialists. During the next three decades, the Austrians won many of their points, and younger members of the class —notably Ludwig von Mises and F.A. von Hayek—introduced several new ideas: they showed the impossibility of central planning in a socialist society, and they explained how credit expansion by government banks causes booms and busts. In 1930, the success of this school seemed assured; by 1950, the school was nearly extinct.

Causes of its death were largely political. The Austrians had demonstrated that intervention would lead to chaos. Naturally, then, Hitler's takeover of Austria made these economists unwelcome in their homeland (Mises' library was seized and destroyed by the Nazis), and many emigrated. About the same time as Hitler's *Anschluss*, Keynesianism —the fountainhead of modern interventionism—gushed forth, easily sweeping aside an uprooted Austrian tradition. Intervention on the practical level had unwittingly combined with its theoretical counterpart to put an end to the Austrian School.

Bleak Outlook

In 1950, few traces of Austrian influence were to be found in economic theory. Moreover, neither Mises nor Hayek, leaders of the school, had a respected academic position from which to extend his influence. Prospects were bleak.

Publication of *The Foundations of Modern Austrian Economics* is an event no one would have imagined 25 years ago. It is a collection of essays written primarily by three economists, Ludwig Lachmann, Israel Kirzner and Murray Rothbard, who have revived the Austrian tradition in America. The Austrian emphasis on the operation of the free market makes this country an appropriate birthplace for the Austrian renaissance.

Economists are gradually realizing that their science has little to say about how the market works. Most of the essays in this volume are meant to correct this defect of economic theory: especially to the point are two essays on the market process by Drs. Lachmann and Kirzner.

The market is seen by these scholars as a great laboratory, where businessmen introduce new products, build new plants, run eye-catching ads, etc., all in an effort to capture profits by better serving consumers. Some of these business experiments succeed, some fail, but the lure of profits insures constant efforts to improve the standard of living.

Amorphous Blob

Businessmen will read the essays on capital with surprise, perhaps with delight. Economists normally eschew capital theory. When they do treat this thorny topic, they commonly assume capital to be an amorphous blob, which they designate by the grand symbol K. How simple the life of the businessman would be if his only worry was whether or not to add a few units of K to his firm.

Instead, he must choose among a wide variety of capital goods that can be combined with each other and with labor in many different ways, and he must choose the combination which will yield the highest return. Mistakes and adjustments are inevitable, and just as they are an important part of business life, so are they an important part of Austrian capital theory.

The essay with the broadest appeal is written by two young economists, G. O'Driscoll and S. Shenoy. They bravely confront what has been an embarrassment to economists—the simultaneous occurrence of worsening inflation and growing unemployment. Neither Keynesians nor Friedmanites had expected it, and their after-the-fact explanations constitute hasty patchwork. According to the main propositions of these economists, inflation and stagnation should not have appeared on the scene together.

Ugly Business

Messrs. O'Driscoll and Shenoy offer a clear picture of "stagflation" (an ugly word for an ugly event), but in so doing they also portray a bleak economic outlook. Inflation and recession are close compan ions, and where we encounte the first, we will sooner or late run into the second. The quote Nobel Laureate Hayek "'Now we have an inflation borne prosperity which de pends for its continuation o continued inflation. If price rise less than expected, then depressing effect is exerted o the economy . . . to slow dow inflation produces a reces sion.'"

Lord Keynes once claime that credit expansion enable governments to perform th miracle of turning stones int bread. The miraculous loaf say the Austrians, is not fit fo consumption. Credit expansio is not a cure for economic illness, but a cause.

Keynesians and their fellow interventionists have clearly failed at economic diagnosis and prescription. Today perhaps more than ever, we badly need sensible advice based on realistic theory. Austrian economists boast both, and the revival of this tradition may yet restore free markets and economic health.

—JACK HIGH