

# Introduction to the Collected Works of Israel M. Kirzner, Volume 1

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## I. Introduction

*The Economic Point of View* was Professor Israel M. Kirzner's first book. Kirzner published the first edition in 1960 with Van Nostrand Press. The second edition was published in 1976 as part of the Institute for Humane Studies series "Studies in Economic Theory". We are using the second edition for this first volume of *The Collected Works of Israel Kirzner* being published by Liberty Fund.

Born in London, UK on February 13, 1930, Israel Kirzner grew up first in England and then in South Africa (between the ages of 10 and 18). He was educated at the University of Capetown (1947-1948), the University of London (1950-51), and then Brooklyn College (1952-54). After graduating from Brooklyn College summa cum laude in 1954, Kirzner came to New York University to earn an MBA in accounting. He earned his MBA in 1955, but while at NYU, Kirzner enrolled in Ludwig von Mises's class on economic theory. In searching for classes to fulfill his course requirements for the MBA, Kirzner examined the university catalogue and the publication list of the faculty. He enrolled in Mises's class for the simple reason that Mises had the longest list of publications among the faculty at the NYU School of Commerce. When Kirzner registered for the class, he was told by administrators and fellow students that Mises was an old man out of touch with the modern world. Kirzner wasn't deterred. From the start Mises's analysis of the market economy intrigued Kirzner, and sparked his interest in the discipline of economics.

After completing his MBA, Kirzner made the decision to study economics in more depth. Mises had advised him to study for his PhD at Johns Hopkins University under the guidance of Mises's former student in Vienna, Fritz Machlup. Mises even offered to arrange a fellowship for Kirzner to study with Machlup as he thought that would be the best path for this promising young scholar of economics. Mises's reasoning was straightforward—Machlup was younger, a renowned and talented teacher, and possessed great professional connections in the world of academics. Machlup would make the path to professional success much easier than it would be studying with Mises. Kirzner decided he would rather stay at NYU and study first-hand with Mises. It is under the influence of Mises that Kirzner came to write on the topic of the definition of economics, as Mises suggested that he explore the various definitions that have been accepted throughout the history of the discipline. *The Economic Point of View* was the result of his doctoral dissertation work done under the auspices of Mises who was Kirzner's mentor and supervisor. Kirzner graduated in 1957 from NYU with a PhD in economics. After

earning his PhD, Kirzner joined the faculty at NYU, where he taught throughout his career.

Two other background issues are important to stress with regard to Kirzner's career in economics. At the time he entered the profession of academic economics, the discipline had been transforming in ways that would come to adversely affect Kirzner's influence.

First, the discipline had moved from a "book culture" to a "journal culture." Scientific contributions were not communicated through books, but through journal articles. Kirzner was a book writer, and what he set out to do once he joined the faculty at NYU was to revise his dissertation into a book, and then to write two other books during the 1960s—*Market Theory and the Price System* and *An Essay on Capital*. It is not that Kirzner did not write journal articles, it is just that these journal articles were not his primary scholarly activity.

Second, the discipline of economics was moving in a direction that increasingly marginalized works in the intellectual history of economics and works that sought to address the fundamental philosophical issues of the discipline, which were the domains of Kirzner's main contributions.

These issues actually fit together—contributions to the history of economics and to philosophy of economics are best communicated in book form rather than the normal science discussions that take place in the journals of the discipline.

It is within this changing context of economic scholarship that Kirzner entered the profession and offered *The Economic Point of View*. Kirzner argues that economics begins with a recognition and then a puzzle. The recognition is that there are systemic forces at work in the market economy that produce social order. This is the "Paris gets fed" idea that Frédéric Bastiat promoted with vigor when explaining what economics is about. The puzzle is how precisely the market economy achieves this degree of social order in the absence of centralized control. The recognition and the puzzle help define the object and subject of the study of economics. As Mises explains in his foreword to the book, "economics shows that there prevails in the succession and interdependence of the market phenomena an inescapable regularity that man must take into full account if he wants to attain ends aimed at."<sup>1</sup> It is hard to think of a more important idea explaining human societies. This fundamental position is at the center of Kirzner's book, in which he carefully explains its emergence and how it came to be accepted. Kirzner provides a historical account of the evolution of the debate and establishes the path that led economics to become the science of human action.

In this introduction to *The Economic Point of View*, we emphasize four crucial aspects that we believe improve the understanding of the book.

First, the context (historical and intellectual) in which the book was published is important. In addition to the shifting context in which scientific contributions were made

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<sup>1</sup> See below Mises's introduction to *The Economic Point of View*.

that we mentioned above, the time of publication was also a period when the object and subject of economics had been totally transformed by the Keynesian revolution. Keynesian macro-theories dominated the mainstream of economic education and economic research by 1960. In that context, Kirzner published a book on the micro foundations of the discipline.

Second, Kirzner argues for a particular form of the microfoundations of the discipline—a consistent and persistent subjectivism. It is only by pursuing the subjectivist position, he argues, that we can aspire to have an objective science of economics. In this sense, he finds himself in the company of Carl Menger, Eugen von Bohm-Bawerk, Knut Wicksell, and Philip Wicksteed in the late 19<sup>th</sup> century, of Mises and Friedrich Hayek in the mid-20<sup>th</sup> century, and to some extent James Buchanan in the later half of the 20<sup>th</sup> century of economic thinking. In the process, Kirzner would eventually seek to establish economic science as occupying the middle ground position between the equilibrium economics of Gary Becker and the indeterminacy of the radical subjectivism of G.L.S Shackle.<sup>2</sup>

Third, the book reveals many of the themes that Kirzner will come to develop later on in his career, especially the nature and role of entrepreneurial activity. We see in the discussion of both catallactics and later praxeology, the essential elements of Kirzner’s theory of the entrepreneurial nature of human action that drives the market process.

Finally, and as Mises explains in his foreword, Kirzner’s work enables us “to re-examine the present state of economic theory in the light of all attempts earlier generations made for their solution. In comparing our point of view with past achievements and errors we may either detect flaws in our own theories or find new and better reasons for their confirmation.”<sup>3</sup> This is especially relevant with regard to the development of behavioral economics and finance in recent years. It is also pertinent to the emergence of neuroeconomics and other related disciplines that are currently influencing the foundational choice theory that contemporary economists work with. The work of Kirzner allows us to reaffirm the foundations of economic science and its relevance to explaining the inescapable regularities of market phenomena. Economics has been under attack from within since the Pigovian and Keynesian revolutions. It is also been under attack from without since the *methodenstreit* at the end of the 19<sup>th</sup> century. The

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<sup>2</sup> This last discussion of situating economics as appropriately occupying the middle ground becomes a major theme of Kirzner work from the mid-1970s onward. As one can see in his critique of plutology and the development of praxeology, the basic pieces of his argument are already present in *The Economic Point of View*. Kirzner’s challenge is to demonstrate how the Ricardian tradition in economics is inappropriate to the task of explaining systemic order because of its focus on the long run impact of technology and resources on economic outcomes. Yet the challenge is also to steer clear of the Keynesian argument that short run fluctuations due to pessimistic and disappointed expectations result in economic chaos. To adequately address the issues raised by (a) the recognition of the existence of a systemic order and (b) the puzzle of how individual purposive behavior can result in this systemic order that we recognize, Kirzner understood that the human element (the calculating as well as the hopes and fears that guide human action) cannot be purged from the analysis. It is in fact, the commitment to a form of scientific subjectivism that unites Mises and Hayek in their understanding of the nature and significance of economic science in opposition to the objectivism of equilibrium always theories, and the nihilism of equilibration never theories.

<sup>3</sup> See below Mises’s introduction to *The Economic Point of View*.

praxeological approach developed by Mises and Kirzner provides the best tools to detect the flaws in new internal or external competing views.

Most dissertations published as books never change the face of economics.<sup>4</sup> Some commentators have seen Kirzner's first book as part of this endless supply of dissertations-turned-into-books which don't address essential problems and don't make much difference to the state of economics.<sup>5</sup> It is true that Kirzner's book is concerned with a problem which generally does not attract much attention: the definition of economics. How do economists define and see their own discipline is a subject that is rarely part of the training that young economists receive. This was already an issue at the time Kirzner studied; it is even more acute today with the quasi-disappearance of the history of economic thought as a subject taught at PhD level. However, almost fifty years after the publication of Kirzner's book, many economists still define the discipline of economics as being about large scale phenomena such as inflation and unemployment.<sup>6</sup> In other words, a determinist and holistic view of the discipline remains common in the 21<sup>st</sup> century despite the microfoundations revolution started in the 1970s. Macroeconomics has left a deep scar on the face of the discipline theoretically, empirically, and even at the conceptual level, and Kirzner's book reminds us that there is a debate worth knowing about.

It would be wrong to consider Kirzner's book as just a book on the definition of economics. Indeed, in trying to provide a definition of economic science, he offers a history of the development of economic thinking. This development takes us from the birth of economics as concerned with the accumulation of wealth to economics as the

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<sup>4</sup> Notable exceptions would include Frank Knight's *Risk, Uncertainty and Profit* (1921), Abba Lerner's *the Economics of Control* (1944), Paul Samuelson's *Foundations of Economic Analysis* (1947), Kenneth Arrow's *Social Choice and Individual Values* (1951), Gary Becker's *The Economics of Discrimination* (1957), and Mancur Olson's *The Logic of Collective Action* (1965). Each of these were viewed primarily as contributions to theory in economics and political economy. But the only book that comes to our mind that was derived from a dissertation that was written self-consciously as one of historical interpretation that has had more than a marginal impact on the discipline since 1950 would be Axel Leijonhufvud's *On Keynesian Economics and the Economics of Keynes* (1968). But even here, Leijonhufvud's influence (along with that of his mentor Robert Clower) was fleeting as the "coordination Keynesianism" he pushed for was displaced by the mid-1970s during the rational expectations revolution and the development of New Classical Economics. Kirzner's book should be classified as lying somewhere between the norm of justified obscurity that is the fate of 99% of doctoral dissertations and the impact (if even just fleeting) that a work such as Leijonhufvud's had in the late 1960s and 1970s. There is something deeply profound about *The Economic Point of View* that might escape more readers on the first read-through but which has kept drawing readers to the work over the years since its original publication.

<sup>5</sup> See for instance Kurt Klappholz's review of *The Economic Point of View* in *Economica*, February 1963, vol. 30 (117), pp. 89-90.

<sup>6</sup> For instance, David Romer in his *Advanced Macroeconomics* textbook (McGraw-Hill Companies, 1996) defines macroeconomics as "the study not just of aggregate fluctuations but of other features of the economy as a whole." (p. 1) Edwin Mansfield's *Microeconomics* (New York: W.W. Norton & Company, Inc, 8th edition) states that "microeconomics deals with the economic behavior of individual units such as consumers, firms, and resource owners; macroeconomics deals with the behavior of economic aggregates such as gross domestic product and the level of employment." (p. 1) Finally, Paul Samuelson in the 16<sup>th</sup> edition of *Economics* (co-authored with William D. Nordhaus and published by Irwin/McGraw-Hill, 1998) states that "economics is the study of how societies use scarce resources to produce valuable commodities and distribute them among different people." (p. 4)

science of economizing behavior. Understanding this development helps us realize the importance of the rise of economics. By understanding the development of economic thinking through the search of the ultimate object of economic science, one comes to see the great accomplishments of early economists. In this sense, the book is more than about a definition of economics, it is a voice in the most important contemporary debates about the nature and achievements of economic science.

## II. The Context of the Economic Point of View

At the time the book came out, Keynesianism defined economics. Strangely, with the exception of a few short passages, Keynes is largely absent of the book.<sup>7</sup> This is because Kirzner focused on the definition of economics, what came to be known as “microeconomics” after WWII. Kirzner did not see the need to address the challenges raised by the discipline of macroeconomics, which was just firmly establishing its hegemony on academic economics at the time he was writing his book. Perhaps it was because once one understands economics either as Robbins defined it or as Mises saw it, there is not much that can be said in defense of the macroeconomic approach.<sup>8</sup>

Many economists trained in the 1950s and 1960s have testified of the split-personality of economics at the time—i.e., the micro-macro split. Metaphorically, on Monday, students would learn price theory (microeconomics) and on Tuesday they would learn Keynesian theory (macroeconomics). For many it was an exercise in contorted logic, which eventually led some to search for the micro-foundations of macroeconomics in the 1970s.<sup>9</sup> Kirzner was in an even more complicated intellectual situation. On Monday, he would learn price theory from George Stigler’s *Theory of Price*, on Tuesday he would learn Keynesian theory and policy, and on Wednesday he would learn Misesian praxeology and market process analysis. Not only what he learnt on Monday would clash with what he learnt on Tuesday but the lessons of Stiglerian microeconomics would also be different from those of Misesian price theory. Read in this context, *The Economic*

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<sup>7</sup> Kirzner ends the chapter on Robbins with a section on the role of economizing in the age of Keynesian macroeconomics. Kirzner is quick to praise the contribution Robbins’s definition can make to the debate. The 1950s and 1960s saw the development of “post-scarcity economics.” With the help of Keynesian recipes, scarcity of means can be overcome and the need to economize disappears. Such a theory, explains Kirzner, denies Robbins’s view of the subject of economics. The Keynesian proposition that “resources may be unemployed for reasons other than the fact that too much is asked for their use” is simply false (Kirzner p. 143). Idle resources are not a sign that economics got it wrong but that the institutional and policy framework is inadequate. Robbins’s definition provides a solid rebuttal against 20<sup>th</sup> century macroeconomics.

<sup>8</sup> We believe Kirzner had the same reaction as that of Hayek in *The Pure Theory of Capital* (1941). Therein Hayek explains that Keynesian economics cannot be considered a serious contender for the dominant role in economic theory because it is a theory which presupposes we are in a world beyond scarcity. This is implied in the idle resources starting point of Keynesian analysis of economic downturns. As a result, Hayek thought the book would be seen as a tract for the times and could not conceivably transform economics as a discipline. Hayek could not have been more off in a scientific prediction.

<sup>9</sup> See *Conversations with Economists: New Classical Economists and Opponents Speak Out on the Current Controversy in Macroeconomics*, Arjo Klamer, ed., Totowa: Rowman and Littlefield, 1984. See especially the conversation with Robert Lucas. This is not to say that the use of aggregates in economics is never appropriate, convenient, or useful. It is to emphasize, as many in the Austrian approach do, that concepts such as “the price level” and “the rate of unemployment” should be very carefully used.

*Point of View* can be seen as Kirzner exploring *which* microfoundations rest at the heart of the discipline of economics.<sup>10</sup>

Kirzner is relatively silent on the micro-macro split that many have talked about, but he expands on the issue of microfoundations. Indeed, understanding the nature of the microfoundations has many implications. For instance, a strict view of the microfoundations in terms of constrained maximization leads to a conception of economics with a strict view of rationality.<sup>11</sup> This is a good tool to explain the market as in an equilibrium-always situation, but it does not help explain the process by which the competing purposes and plans of individuals come to be reconciled through market exchange.

Another important issue is the nature of scientific inquiry, which has evolved since the 19<sup>th</sup> century towards an empiricist and positivistic approach.<sup>12</sup> Strict positivism rejects any reference to individual purposes and plans and advocates instead observing the (direct or indirect) results of human activities by means of statistical testing. It follows that an essentialist and axiomatic-deductive (a-priori) approach is not regarded as providing any valid knowledge about reality.

In contrast, Kirzner explains that “[t]he search for the precise nature of economic theory becomes of importance simply because it offers proof that economics *has* a ‘nature of its own’.”<sup>13</sup> To most modern economists, the search for the true nature of their subject is a useless endeavor. Kirzner instead offers to thoroughly examine the issue. We find here the essentialist aspect of Kirzner who not only thinks that the essence of a phenomenon exists but also that it is a worthwhile endeavor to try to establish it. This permeates his

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<sup>10</sup> On the genesis of these ideas in Kirzner’s system, see for instance his unpublished speech given for his FSF-Nutek Award in 2006.

<sup>11</sup> See below in section III the debate between Kirzner and Becker.

<sup>12</sup> On this point, see below Laurence Moss’s introduction to the second edition of *The Economic Point of View*. For critiques of this turn in economics toward empiricism and positivism (from the perspective of the Austrian School of Economics) see Hayek, *The Counter-Revolution of Science* (1952) and Mises, *The Ultimate Foundations of Economic Science* (1962). In his preface to the second edition of Mises’s *The Ultimate Foundations*, Kirzner explains the link that Mises drew from the philosophy of science to the nature of economic science to public policy. “Mises directed a withering barrage against the illegitimate extension to the realm of social phenomena of the methods and modes of thought appropriate only to the natural sciences. In human affairs, he insisted, we cannot dispense with the category of the mind, with reason, with purpose, and with valuation. To attempt to grapple with the phenomena of society without recognizing the role of purposeful, rational individual human action is a vain and misguided endeavor.” (Kirzner 1976, p. vi-vii) But as Kirzner points out, Mises’s point has more importance for the enterprise of economics than is normally realized. It is not just the blind alley that positivism leads one down that bothered Mises, but that positivism followed consistently in the field of economics would discredit the discipline. As Kirzner put it: “Mises saw the denial of economics as an alarming threat to a free society and to Western civilization. It is economics that is able to demonstrate the social advantages of the unhampered market. The validity of these demonstrations rests heavily on precisely those insights into individual human action that positivist thought treats, in effect, as meaningless nonsense. What inspired Mises’ vigorous and spirited crusade against the philosophic underpinnings of an economics not founded on human purposefulness was more than the scientist’s passion for truth, it was his profound concern for the preservation of human freedom and dignity.” (ibid.)

<sup>13</sup> See Kirzner, p. 9.

work from the definition of economics to the definition of entrepreneurship. While defining the essence of an economic phenomenon may at times be a pointless exercise when done for its own sake, Kirzner sees this as the first step in a chain of reasoning that provides a greater understanding of reality. It is precisely because Kirzner examines the essence of economic theory that he is able to define the content of praxeology and to establish its theorems.

### **III. Subjectivism as the Foundation of an Objective Science of Economics**

The main theme of Kirzner's book is that the evolution of economics can be understood as the evolution of the idea of subjectivism.<sup>14</sup> Economics started as a quasi-objective science—it was objective in the sense that the ends that individuals pursue were taken as objective data for the economist—and evolved into a science perfectly incorporating individuals' subjective valuations. In a somewhat ironic twist, Kirzner's argument is that it was only by pursuing the consistent subjectivist line, where the content of ends is unquestioned and the analysis is limited to one of the examination of the effectiveness of chosen means in satisfying given ends, can the science of economics aspire to objectivity. This was the understanding of the value-free (*wertfreiheit*) nature of the sciences of human action championed by Max Weber and Mises in the early years of the 20<sup>th</sup> century and which established economics as a positive science as opposed to a normative endeavor. *The Economic Point of View* is largely a narrative of the evolution of this position and, in the process, juxtaposes the classics (John Stuart-Mill) with the moderns (Mises), and offers implications for the debate between the moderns and the contemporaries (Paul Samuelson and George Stigler) circa 1950-1960 economics. In this section, we examine the evolution of the idea of subjectivism as Kirzner explains it in the book.

#### *The Science of Wealth*

Economics considered as the science of wealth is the result of the search for objective criteria upon which economists could build their discipline. In this tradition, we find Adam Smith, the Earl of Lauderdale, T. R. Malthus, and Nassau Senior struggling to find an objective definition of wealth which would satisfy the requirements of economics. Should only material wealth be included? If so, what constitutes wealth for some may not for others. Economists could not find a way to come to an agreement. There were many rebellions against the conception of economics as the science of wealth, but no one at the time fully understood the problem.<sup>15</sup>

#### *The Science of Avarice*

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<sup>14</sup> Kirzner echoes here Hayek's famous statement: "It is probably no exaggeration to say that every important advance in economic theory during the last hundred years was a further step in the consistent application of subjectivism." In *The Counter-Revolution of Science*, Glencoe: The Free Press, 1952, p. 52.

<sup>15</sup> One attempt was to introduce the notion of welfare to replace that of wealth. However, as Kirzner explains, the use of the conception of welfare was not much different from that of wealth for the reason that it was mostly welfare as in "material well-being" that was studied.

Economics considered as the science of avarice studies what it regards as the most powerful human motives: self-interest. The connection between economics and selfish behavior had long been implicitly assumed but became explicit as economists engaged in the study of wealth. The important result of this line of thought is the emergence of *homo oeconomicus*, the economic man whose motives are self-centered and whose activities revolve around wealth accumulation. This approach, Kirzner explains, establishes specific “economic” motives and ends that people supposedly pursue. Here again, economists such as Walter Bagehot, Robert Lowe, W. Cunningham, and F. Y. Edgeworth tried to establish economic science ignoring on the whole the importance of the subjective element in human motives.

An important contribution of Kirzner was to emphasize the work of Philip Wicksteed on human motives. Wicksteed saw no role for specific “economic motives” and defined economic relationships in terms of “non-tuism.” The key here is the distinction between motives (or interest) and purposes. Two parties may enter into an economic relationship with each intending on furthering his or her own purpose. However this purpose may not be selfish, but rather entirely altruistic. For instance, a mother may want to buy milk at the lowest price possible in order to feed her baby. As Kirzner points out, “Wicksteed’s rejection of egoism allowed him to include under ‘one’s own purposes’ every conceivable interest.”<sup>16</sup>

### *The Science of Money*

Economics as the science of money is another attempt to objectify individuals’ ends. The problem was not so much to define money, but assert that money is an objective and universal measuring rod. Among those who attempted to see measurement of utility at the core of economics was the great Alfred Marshall—although his obsession was more with measuring motives. Money prices reflect (to some degree at least) human preferences and thus in that sense convey information. The money price of a good expresses the market actors’ preferences for this good over a whole array of alternatives. However, this does not mean that the resultant prices offer an (objective) measure of human preferences and motives. In this sense explains Kirzner, “money has never in any but the crudest of sense been able to serve as... a measure [of utility].”<sup>17</sup> As the other approaches described above, this view comes short of providing a general approach to economic phenomena and instead is limited to a certain class of objects (money) or a special human condition.<sup>18</sup>

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<sup>16</sup> Kirzner, p. 66. After Wicksteed, it became more difficult to sustain that economics is the science of *homo oeconomicus* driven by self-interest. However, this approach persisted among economists for an entirely different reason: the rise of the mathematical method also known at the time as the “mechanics of utility” pioneered by William S. Jevons and Francis Edgeworth. This mechanical conception of economic activity relied on the construction of the self-centered economic man. As Kirzner puts it: “the roots of the mechanical conception of economics... go back as far as the ascendancy [sic] of self-interest in economics and its translation into the maximization-pattern of behavior in a form amenable to mathematical treatment.” Kirzner, p. 70. See also Mises, *Human Action*, pp. 62-4, and Hayek, *The Constitution of Liberty*, Chicago: The University of Chicago Press, 1960.

<sup>17</sup> Kirzner p. 100.

<sup>18</sup> In monetary calculation, money prices represent an objective measure of subjective valuations. In this sense, money is a measuring rod. However, knowing what the relative money price of a good is does not provide a measure of the subjective valuations of others. It merely reflects them. It follows that money

### *The Science of Economizing*

With Lionel Robbins comes a new way of thinking about the discipline. It all started with the notion of scarcity. “With the movement away from the objectivism of the classical science of wealth and with the increasing interest, during the second half of the last century, in man and his behavior,” explains Kirzner, “the idea of scarcity as a factor conditioning human action assumed ever greater importance.”<sup>19</sup> Scarcity was omnipresent in Carl Menger’s analysis as well as in Walras’s, but it became even more central with Robbins. Two more ideas enabled the development of Robbins’ view. First, the emphasis some economists put on the idea of “maximization.” Second, the relevance of the means-ends framework as a description of what economists should focus on. Once Robbins combined these three elements—scarcity, economizing, and means-ends—he was able to focus on an *aspect* of human action rather than a particular *kind* of human action. That aspect of action is the act of economizing scarce means that have alternative uses to pursue multiple ends. For the first time, a definition was ethically neutral, i.e., economists didn’t ascribe any regard to the end pursued. Fully integrating subjectivism into economic science could now be contemplated.

While Robbins’s definition opens the door to a truly subjectivist approach in economics, it is not entirely satisfying. Kirzner points out that the concept of purpose is excluded from Robbins’s view. Ends are different from purpose; they are “tendencies to conduct.” Individual economic activity is not driven by conscious aims, but by tendencies that are “objective ‘pulls’ similar to physiologically conditioned ‘needs’.”<sup>20</sup> The absence of purpose is reminiscent of the mechanical conception of economic activity and *homo oeconomicus*. By removing purpose out of action, Robbins made ends (and means) more concrete than they are in reality. As Kirzner puts it, “ends can be conceived as observable states of affairs only *after* their achievement. At the time of the contemplation of action, ends are to the actor only anticipations of future hoped-for states of affairs.”<sup>21</sup> Though it establishes the approach that would allow subjectivism, Robbins’ framework eventually rests on objective means-ends.<sup>22</sup> This is because it expunges purpose from human action.

### *Praxeology or the Science of Human Action*

Going beyond Robbins’s limitations is Kirzner’s goal in the last chapter of *The Economic Point of View*, which focuses on the praxeological understanding of economics. This chapter, by its breadth, shows Kirzner’s remarkable mastery of the subject at a young age. The fundamental idea of praxeology is that beyond the facts of physiology,

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cannot be a universal measuring rod used in economics to know utility levels. It can only be an objective rod reflecting the size of the subjective trade offs one makes when choosing.

<sup>19</sup> Kirzner, p. 111.

<sup>20</sup> Kirzner, p. 130.

<sup>21</sup> Kirzner, p. 125.

<sup>22</sup> For instance, Robbins explained that economics is characterized by the problem of multiple ends. However if ends can be compared because given wants (i.e., preferences) enable the ordering of ends separate from the act of economizing, then there is really only one end that the actor pursues. If there is only one end (an “objective pull”), then human action is reduced to a mechanical conception in which choosing is artificial.

psychology, and physics, there remains a scientific explanation of human action.<sup>23</sup> This explanation rests on “the implications of the rationality that governs purposeful behavior.”<sup>24</sup> In this sense, economics purports that all action is purposeful and that the same rational principle governs all conscious human activities.

### *Subjectivism and Rationality*

Kirzner also explains the link between purpose and rationality. The concept of rationality, writes Kirzner, “exists for praxeology only as the expression of human purposes.”<sup>25</sup> For Kirzner, action is rational by definition. This contrasts with a more Robbinsian rationality, which involves the automatic selection of means into a pattern corresponding to the final hierarchy of ends.<sup>26</sup> In the eyes of many economists, Kirzner’s view makes rationality useless for economic theory. In this sense, it is preferable to accept that individuals are not always cool calculators and that sometimes they can be under the pernicious influence of passion or other “irrational” motives. However, Kirzner contends that even during the moments where a man gives in to temptation or is under the spell of emotions, he is still acting as a human being directed by reason. Economic theory as the science of human action is concerned with one universal aspect of human action, that of consistently pursuing one’s own purpose, irrespective of how often these purposes change or how inconsistent they are with some greater goals that the individuals has selected for himself.

The consequences of Robbins’s view are most manifest in the idea of rationality in economics. A rational individual allocates the most adequate means to achieve her most desired end in a perfectly efficient way. However, as Gary Becker argued, even if one were to assume rationality away, market results would still be rational.<sup>27</sup> In other words, even if some individuals are assumed not to react to price changes the way a rational being would, they are forced by the nature of the opportunity sets they face (after a relative price change) to alter their behavior. In what became an important debate, Kirzner replied that Becker implicitly assumed that individuals pursue objectives and thus are rational.<sup>28</sup> Indeed, what Becker describes as an alteration of behavior is really the market process at work.

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<sup>23</sup> The exact quote is: “because man possesses the power to reject one course of action for another, to arrange the satisfaction to be derived from obeying specific impulses within a wider ordering of values, the physical, physiological, and psychological sciences do not exhaust the facts of action that are capable of scientific explanation” Kirzner, p. 151.

<sup>24</sup> Kirzner, p. 151.

<sup>25</sup> Kirzner, p. 166.

<sup>26</sup> Economizing is, of course, part of the praxeological approach to economics. However, economists in this tradition see it as economizing as done by human actors, not automatons. It is economizing within an open-ended universe and not a closed system. To ensure determinacy in explanation, the economizing aspect of human action was translated into maximizing behavior by machines and within a closed system in which ends were fixed.

<sup>27</sup> See Gary Becker, “Irrational Behavior and Economic Theory,” *The Journal of Political Economy*, vol. 70, No. 1, Feb. 1962, pp. 1-13.

<sup>28</sup> See Israel Kirzner, “Rational Action and Economic Theory,” *The Journal of Political Economy*, vol. 70, No. 4, Aug. 1962, pp. 380-85. See also Gary Becker, “Rational Action and Economic Theory: A Reply to I. Kirzner,” *The Journal of Political Economy*, vol. 71, No. 1, Feb. 1963, pp. 82-3. And Israel Kirzner,

The consistent pursuit of subjectivism leads Kirzner into the following position. Economics is concerned with the acting man. Human action is purposeful and the only way to understand this issue as an economist is to adopt a fully subjectivist position. It is only once subjectivism is acknowledged that one can explain individual action as the pursuit of subjective purposes, the values of which are only known to the individual at the time of action.

Becker, by trying to avoid being entangled into the problem of imposing an external definition upon rationality, throws out the baby with the bath water. The propositions of economics, however, cannot be obtained if one assumes away any form of rationality (i.e. purpose). Conversely, there is no need for the same propositions to establish an external benchmark against which the rationality of every agent would be judged. It is enough to posit that action is purposeful.

The same is true of the radical subjectivist position, which contends that economists cannot establish the existence of market regularities for they can only be demonstrated by objectivizing certain subjective data of human action. However, the solipistic position à la G.L.S. Shackle as developed in his *Epistemics and Economics* (1973) is overcome because in the Mises-Hayek-Kirzner understanding of the price system, the subjective evaluation of trade-offs by some individuals become objective terms of trade utilized by others in making their subjective evaluation of trade offs. The essence of monetary calculation is to be found in the translation of subjective trade offs into objective terms of trade in such a manner that economic actors by employing the mental tool of monetary calculation are able to sort out among the numerous array of technologically feasible projects those which are economical (i.e., cost effective). This is why Mises argued that only the development of the subjectivist perspective could lead to the recognition of the problem of economic calculation.<sup>29</sup> Equilibrium theorizing solves the problem by hypothesis, solipicism has no solution to the problem. However, praxeology (including market process theory) respects subjectivism of value and of expectations, and yet highlights the mental tool of monetary calculation and the discipline of profit and loss to lead to continuous adjustments to exhibit an inescapable regularity.

Kirzner's development of the subjectivist position puts him in the middle ground.<sup>30</sup> This is an important theme that emerges early in Kirzner's career and is already present in *The Economic Point of View*. Kirzner does not situate economics within Shackle's view, nor does he locate it with Stigler (standard rationality) or Becker (expunging rationality). He shows that a thoroughly subjectivist position is possible without having to compromise

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"Rational Action and Economic Theory: Rejoinder," *The Journal of Political Economy*, vol. 71, No. 1, Feb. 1963, pp. 84-5.

<sup>29</sup> As Mises put it: "To understand the problem of economic calculation it was necessary to recognize the true character of the exchange relations expressed in the prices of the market. The existence of this important problem could be revealed only by the methods of the modern subjective theory of value." *Socialism*, Indianapolis: Liberty Classics, 1981, p. 186.

<sup>30</sup> See Roger Garrison, "Austrian Economics as the Middle Ground: Comment on Loasby," in Israel Kirzner, ed., *Method, Process, and Austrian Economics: Essays in Honor of Ludwig von Mises*, Lexington: Lexington Books, 1982.

on the explanatory power of economics as Shackle does and without having to impose an external benchmark on human action.

*The Economics of Men and Rats*

James Buchanan is among the few economists who have noticed the divide between a strict application of rationality and one that is the result of subjectivism. In a paper written in honor of Mises, he makes the distinction between “predictive economics” and what he calls “subjective economics.”<sup>31</sup> He finds that there is a “legitimate domain for predictive economic theory” but in this understanding of economic behavior, “men are like rats.”<sup>32</sup> On the other hand, “subjective economics offers a way of thinking about economic process, a means of imposing an intellectual order on apparent chaos without inferentially reducing the status of man, as a scientific object, to something that is not, in kind, different from that of animals.”<sup>33</sup> In Buchanan’s view, men act sometimes as rats and sometimes as creative beings. Thus in his view, we need two types of economics to understand the two different types of behavior.

While Buchanan sees what most economists who subscribe to the standard rational choice framework do not see (namely that man is a creative being and that this fact can only be explained by allowing a full subjectivist understanding of economics), he does not accept the idea that this could be done with the help of a single coherent body of economic propositions. For Buchanan, the alternative presented to us is Beckerian determinacy on the one hand and Shacklean indeterminacy on the other. There is no viable middle-ground position between these two approaches. What we gain in philosophical understanding with the Shacklean position, we sacrifice in scientific precision. On the other hand, what we gain in scientific precision with the Beckerian position, we sacrifice in philosophical understanding of the complex nature of the human drama of imagination and choice. In other words, in Buchanan’s formulation economists can be philosophically astute but at the expense of scientific prediction, or we can provide scientific prediction but only at the expense of philosophical understanding of the matter under investigation.

The idea of a philosophically sophisticated yet scientifically rigorous economics is beyond our grasp in the study of human action according to Buchanan. As a philosophical pragmatist of some stripe, this predicament does not concern Buchanan—when the questions are of philosophical importance we can address man as a creative creature, but when the questions are more routine we can treat man as if he were a rat. In this, as in almost everything in Buchanan’s work, the “relatively absolute absolute” enables him to avoid making the strict choice he suggests we must make. Despite the fact that perhaps there are no contemporary theorists in economics and political economy of high professional stature closer to the position of the Austrian school than James Buchanan, Kirzner’s position represents a different turn than that offered by pragmatism.

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<sup>31</sup> See James Buchanan, “The Domain of Subjective Economics,” in Israel Kirzner, ed., *Method, Process and Austrian Economics*, 1982, Lexington Books. All references to Buchanan, unless otherwise stated, are to “The Domain of Subjective Economics.”

<sup>32</sup> See Buchanan, p. 15.

<sup>33</sup> See Buchanan, p. 16.

Kirzner instead argues that praxeology provides a body of theory fully consistent with the subjectivist position and that is necessary and sufficient to explain human action in all circumstances. Kirzner provides a way out of the false alternative Buchanan set up.<sup>34</sup>

The reason why Buchanan clings to the neoclassical view is that he believes that the search for empirical regularities in human conduct can only be carried out if we uncover the side of human action where men are like rats. It is the great achievement of the Mises-Hayek-Kirzner approach to show that the regularities of market phenomena can only be fully understood within the domain of pure subjectivist economics where individuals are fully human, capable of creation. Buchanan thinks these regularities can only be demonstrated empirically, while Mises, Hayek, and Kirzner show that they can be established through the use of praxeological reasoning.

#### **IV. The Premises of Entrepreneurship Theory**

Understanding the development of economic thinking establishes the foundations for the development of future theories. It is also Kirzner's participation in the debates of his time that nourished the subsequent development of his thinking. Indeed, *The Economic Point of View* is full of insights that Kirzner developed later on in his life. Most of all, it is precisely because of his intimate knowledge of the discipline—especially the emergence of subjectivism in economics in the first part of the 20<sup>th</sup> century—that Kirzner was able to develop his theory of entrepreneurship and the market process.

As we mentioned above in the debate with Becker, Kirzner clearly explains his position in terms of market process. For instance, he uses terms such as “discovery” and “realization.”<sup>35</sup> The praxeological position naturally led Kirzner to understand the market as a process in which people can make errors, but also one in which people tend, because of their rationality, to correct them.

By the time Kirzner wrote *The Economic Point of View*, his theoretical foundations were already deeply rooted in the subjectivist approach of purposeful human behavior. This perspective is uniquely suited to explain entrepreneurial activity. Entrepreneurship involves the recognition of a new means-ends framework, rather than diligently working within the existing means-ends framework to maximize returns. As a result, the entrepreneurial decision structure must be open-ended. In this sense, a strict approach such as that of Robbins or George Stigler limits the economizing of actors to what they already know. Economics in Robbins's view does not allow the discovering a new means-ends framework. Robbinsian economics is about studying the activities of men engaged in solving an allocation problem by understanding the conditions under which

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<sup>34</sup> Max Weber, like Buchanan, understood the existence of subjective economics through his *verstehen* approach. For Weber, action is purposeful and human beings are capable of creative action. However, this was not sufficient, in his view, to see economic behavior in every human action. To this end, he devised an artificial abstraction, the ideal type, which represents the man to which economic laws apply. A problem with the ideal type is that it makes the universality of economic propositions impossible, as they are restricted to the ideal-type case. Buchanan and Weber share the view that for economics to be predictive, it has to apply to a specific type of human beings. See Kirzner pp. 157-9.

<sup>35</sup> See Israel Kirzner, “Rational Action and Economic Theory,” Op. cit.

this problem comes to be resolved. This study assumes available means that have alternative uses and already identified ends. In contrast, entrepreneurship involves both the identification of new ends as well as the recognition of new means to achieve these new ends.

For new means-ends decision frameworks to be identified, the economizing principle must be “flexible” enough. This is the reason why the two concepts of “purpose” and “subjectivism” are essential to informing the context in which human rationality operates. Kirzner noted the absence of purpose in Robbins’s framework. Purposefulness involves choice but also involves an active participation of the individual, such that it is more than just a passive choice among already-known alternatives. Purposefulness allows the idea of discovering what one’s purpose in action is. It enables open-endedness. This openness includes the problem-solving capacity of human beings for instance.<sup>36</sup>

Subjectivism pervades Kirzner’s analysis of human action, which sets the framework for the economics of entrepreneurship. For instance, he states that ends are not “data” but purposefully chosen and subjectively perceived goals. In praxeology, the selection of ends as well as the selection of means (which are just more proximate ends) is an issue of judgment that is not automatic and it becomes only fully recognizable after the facts.<sup>37</sup> It follows that rationality can only be understood as infused by the purposefulness aspect of human action and the subjective valuations of actors.<sup>38</sup>

There is another aspect of the praxeological view of rationality that has important consequences for entrepreneurship and the issue of regularities of market phenomena. This is the idea that there is “no room for any discrepancy between the conception of a program and its realization; the two concepts coincide completely.”<sup>39</sup> In other words, giving in to the temptation of, say, drinking wine means that the end (i.e., the program) has changed and new means are being used to pursue this new end.<sup>40</sup> However, this also means, in Kirzner’s view, that actions can be judged with regard to an earlier program. Kirzner stipulates a tendency in human beings to stick to the (already-initiated) program. The role this tendency plays in Kirzner’s system seems to be mostly empirical. The

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<sup>36</sup> See Kirzner: “Within narrow limits man can be observed and his behavior explained purely mechanically. At this level of interpretation human behavior is considered only in the positive terms of stimulus and response; it is completely “caused” in the sense that the problem-solving elements in human conduct are ignored” p. 176-7.

<sup>37</sup> Kirzner states that “in the concept of economy, ends and means constitute a scheme more or less artificially imposed on action so that the relative valuations of ends can be reflected in the specific pattern in which resources are allocated” p. 161. Moreover, “‘means’ exist as such for the acting man only after he has turned them to his purpose; acting is not apportioning, but doing—doing what seems likely to further one’s purposes” p. 162.

<sup>38</sup> Kirzner states that “It is only from ‘outside’ that... rationality can be described merely in terms of a particular pattern of resource allocation. The full praxeological grasp of human action perceives its rationality as completely pervaded by the ‘aiming’ quality bestowed on action by its teleological character.” Kirzner, p. 166.

<sup>39</sup> Kirzner, p. 171.

<sup>40</sup> Drinking Rhenish wine was the example Vilfredo Pareto and Benedetto Croce discussed. Kirzner p. 169.

existence of a tendency to stick to a given program makes it possible to apply economic reasoning to actual situations.<sup>41</sup>

The existence of tendency to stick to already-initiated programs is not to be confused with the constancy of wants. The idea that preferences are given is something that economists—including praxeologists—readily accept. Robbins, for instance, acknowledged the constancy of wants if economists were to make sense of the world. This theoretical position, however, does not imply that ends cannot change. This is where the entrepreneurial role is most relevant. Entrepreneurs reveal new ends and new means which are compatible with wants that are supposed to be given but were hitherto unexpressed. Praxeology offers a framework in which the entrepreneurial aspect of human action can explain program changes. Program changes must be such that they don't make the whole application of economics impossible. Programs change but are sufficiently stable to create a social order where patterns of behavior can be relied on to a large extent.

Finally, Kirzner expresses a preference in favor of the “economizing principle” over the “maximization principle” in Robbins’s work. The idea of maximization implies an ultimate end that can be meaningfully maximized (i.e., squeezing as much satisfaction out of the available means to obtain this end). Economizing only assumes that individuals carefully use the scarce means available in the face of competing arrays of ends that are not automatically selected. Economizing enables an open-ended choice framework in which individuals come to select the means they want to pursue. Economizing is compatible with the subjectivist open-ended framework necessary to the economics of entrepreneurship.<sup>42</sup>

## V. The Challenges of Behavioral Economics

*The Economic Point of View* provides a perspective helping locate the theories of the Austrian school within the development of economics in the second part of the 20th century. This is especially true with regard to the role methodological subjectivism and

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<sup>41</sup> As Kirzner explains: “By taking a cross section of social phenomena at a particular instant in time, by considering the programs that members of society have chosen at that instant and by mentally arresting program changes, one can apply praxeological theorems to these various programs and deduce the consequences. The conclusion so derived are valid in relation to the assumed programs, and provide an explanation of the concrete phenomena of the real world in so far as there *is* a tendency for men to adhere to programs once they have been initiated” p. 175. Kirzner provides the example of a city. If one of the means of transport to access the city is crippled for some reason, people will seek alternative means of transport. An external observer can come to this conclusion (that people will seek alternative means of transport) because he assumed that people desire transportation and that this was not bound to change in the near future. In other words, it is only in relation to the knowledge of a given purpose that economics can be applied to the actual world. Mises also emphasized the idea that it is only by abstracting from change that one can explain economic phenomena. A major issue for applied economics is to find a way to access the “programs that members of society have chosen.” This is, in part, the goal of history. See also the interview Kirzner gave to *The Austrian Economic Newsletter* in 1997.

<sup>42</sup> Although Kirzner says that Robbins used both notions of economizing and maximizing, Kirzner employed the expression “Robbinsian maximizing” in his later work, denoting the closed character of Robbins’s definition.

methodological individualism play in modern economics. As Murray Rothbard mentioned in his review of Kirzner's book, economics is profoundly different from other social sciences.<sup>43</sup> Recent developments, however, have put this distinction in jeopardy, as more and more economists are striving to incorporate "behavioral" elements taken from other sciences in economic theory in the hope to improve the conclusions of economic thinking.<sup>44</sup> Kirzner's work helps us explain the significance of this new approach.

Behavioral economics applies the results of cognitive science and psychology to the field of economic theory to better understand how market outcomes are affected by imperfect human decisions. Its main goal is to examine the notion of rationality and whether this assumption has any counterpart in the reality of human behavior. This directly relates to Kirzner's discussion of rationality in economic science. Kirzner painfully carves out what he sees as being the core of economic behavior by establishing that beyond the explanations of physiology, psychology, and physics (which may be true in so far as they affect human behavior), there remains an explanation that is purely the result of the fact that humans act.<sup>45</sup> Even during the moments where emotions seem to dictate action, human behavior is directed by reason in the sense that an individual has a purpose and subjectively values the means at his disposal to achieve subjectively selected ends.

Neoclassical economics fundamentally misconstrues both human choice and market equilibrium and the relationship between them. Historically, to make the model tractable with calculus, the functional form of behavior and interaction had to be represented in a formula that was continuous and twice differentiable in order to render optimality results within the model. This entailed imbuing economic actors with almost unlimited cognitive capabilities and putting them in very simple environments. Under these conditions, the

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<sup>43</sup> See Rothbard's review of *The Economic Point of View in Modern Age*, Spring 1961, pp. 203-4.

<sup>44</sup> See John Davis "The turn in economics: neoclassical dominance to mainstream pluralism?" *Journal of Institutional Economics*, 2 (1), 2006, 1-20. Davis argues that game theory, experimental economics, behavioral economics, evolutionary economics and non-linear complexity theory are supplanting the neoclassical research program of constrained optimization and general competitive equilibrium. Some may see this as an opportunity for Austrian economics to gain more prominence. See in particular Roger Koppl's paper "Austrian Economics at the Cutting Edge," *Review of Austrian Economics*, 19 (4), 2006: 231-241. Koppl sees bounded rationality, rule following, institutions, cognitive, and evolutionary economics as the future of research in core economic theory. The good news is that the Austrians are already there. Alternatively, it could be argued, as Davis does, that the breakdown in the neoclassical hegemony has not led to a new pluralism in economics because certain types of heterodox economics are excluded—there is a selective appropriation process that is going on. See also Peter Boettke, Christopher Coyne, and Peter Leeson "Man as a Machine: the Plight of Twentieth Century Economics," *Annals for the Society of the History of Economic Thought*, June 2003, 1-10, where the authors describe the modern intellectual situation in economics as best understood as one of formalistic historicism.

<sup>45</sup> As Kirzner puts it: "The contribution that the praxeological point of view has made to the scientific explication of action in history is the isolation of an element in action the explanation of which is not exhausted by even the most complete application of the sciences concerned with the concrete manifestations of human action. This residual element is that of the operation of human action itself, which neither is explained by physical, physiological, or psychological theories nor requires the assistance of these doctrines for its own exposition. A praxeological science, using the rationality of human action as its foundation, is able to derive theorems describing the path of action under given circumstances. The reasoning that constructs these theorems mirrors the reasoning that is implied in action itself. New links in the chain of knowledge, in the form of praxeological theorems, are forged from the constraint that human purposefulness imposes on action, namely, that it be taken only with the sanction of reason." p. 150-1.

results of maximizing and competitive equilibrium flowed naturally. This characterization of the economic system, as critics never tired of pointing out, was wildly unrealistic. The messy details of economic life were avoided and instead agent omniscience assured that the coordination of economic activities would be achieved effortlessly. Any deviation from the assumptions of agent omniscience or the uncomplicated environment, however, and the market system would fail to generate optimal results. Microeconomics in the 1950s and 1960s strove (a) to develop an institutionally antiseptic theory, and (b) to articulate a theory of market failure (when the conditions that made that pure theory of economic equilibrium possible were violated). Either cognitive limitations on the part of actors or imperfections to the market structure were enough to result in deviations from the ideal.

The neoclassical model of human choice in the 1960s and 1970s was generalized to a variety of human endeavors outside the normal confines of market exchange. The development of the economic analysis of law, politics, and the family under the rubric of 'economic imperialism' was perhaps the most intellectually exciting work in the mainstream of economic research during that time. With the development of rational expectations theory in the 1970s and the subsequent victory of New Classical Economics over Keynesian macroeconomics the core model of maximization, stable preferences, and market equilibrium was firmly in place as the economic point of view. From the point of view of the methodological individualism espoused in Kirzner's *The Economic Point of View*, this development could not be completely bemoaned. But from the more subtle point of praxeology, this history was indeed disturbing.

Modern behavioral economics is a reaction against the sterility of the neoclassical hegemony of maximization, stable preferences and market equilibrium. It mostly describes the results of laboratory experiments in psychology and other related disciplines. Economists such as Richard Thaler and psychologists such as Daniel Kahneman and Amos Tversky pointed out how people deviate from the model of rational choice in making their real life decisions. Instead of ruthlessly maximizing utility subject to constraints, their emotions and states of mind would get the better of them. As a result, systemic biases emerged in choice making which prevented optimal choices from being made. Real human choosers, rather than artificial agents in a rational choice model, suffer from status quo biases, loss aversion, and self-serving penchants in such a manner that market efficiency cannot be realized in practice. In this approach, "anomalies" unaccounted for in the norm of perfect markets are in fact the reality of economic life.

This reading of the results of behavioral economics constitutes a significant challenge to the economic point of view. Three responses to the behavioral challenge have emerged in recent years in the literature of economics. The first response stresses that laboratory experiments do not do as good a job as we would like in approximating real world choice conditions. Therefore, what might appear as anomalous results are instead to be explained by the experience of the students outside of the laboratory or contamination inside of it. Moreover, the artificial situations created in the laboratory do not capture the stakes involved in real life decision making. When the stakes are sufficiently high, and the data comes from field experiments (as opposed to laboratory settings), economists such as

John List have argued that economic actors behave in a fashion quite consistent with the *homo oeconomicus* model of man.<sup>46</sup> In other words, in those situations where the choices are real and the stakes are such that people have to pay the cost for poor decisions, they will more often than not choose in a way consistent with the standard economic model. List's basic finding is that people learn their way out of the biases in decision making through experience in the relevant market. The decision biases that Kahneman, Tversky and Thaler find in the laboratory are relevant for inexperienced economic actors (such as college students), but do not capture the behavior of actual actors and experienced traders in particular markets (such as baseball cards, or stocks and bonds).

The second response was given by Vernon Smith, one of the founders of experimental economics and Kahneman's co-Nobel Laureate in the field. In Smith's view, the perceived anomalies are "ecologically rational" despite being inconsistent with the scientist observer's own judgment of what constitutes "constructively rational" behavior.<sup>47</sup> The basic point Smith stresses is that rationality manifests itself in a variety of manners depending on the context of choice. Choices are never made in a vacuum, but always within a specific context. Smith emphasizes the importance of reciprocity and promise keeping in the development of exchange and trade. In order to take from someone, one also has to give. In the context where this basic rule is violated, the outcome of rational choice will be different. It is only where takings (without reciprocity) are prohibited that prosperity materializes. But the rationality of the decision maker is not questioned in either context, however different they are. The consequences of rational choice are dependent on the environment within which the choices are made.

The third response to the challenge of behavioral economics is to stress the subjectivity of ends that heterogenous actors possess in the economic system.<sup>48</sup> The Mises-Kirzner point is that choice is an open-ended process of discovery where, not only are human actors learning how best to arrange means to obtain ends, but also which ends are worthy of pursuit. Again what might appear as anomalous results are in fact economic actors

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<sup>46</sup> See John A. List "Does Market Experience Eliminate Market Anomalies?," *Quarterly Journal of Economics*, 2003, 118(1), 41-71; and "The Behavioralist Meets the Market: Measuring Social Preferences and Reputation Effects in Actual Transactions," *Journal of Political Economy*, 2006, 114(1): 1-37.

<sup>47</sup> See Vernon L. Smith, "Human Betterment through Globalization," Foundation for Economic Education, September 2005; and "Constructivist and Ecological Rationality in Economics," *American Economic Review*, 93(3), June 2003, pp. 465-508.

<sup>48</sup> This subjectivity point is also why praxeology would resist what is becoming known as "neuroeconomics." See Colin Camerer, George Lowenstein, and Drazen Prelec "Neuroeconomics: How Neuroscience Can Inform Economics," *Journal of Economic Literature*, vol. 43, no. 1, March 2005, pp. 9-64. To be clear, it is not to deny that neuroscience is fundamental to understanding human health, it is a denial that neuroscience is particularly helpful in the field of praxeology. The reason is straightforward, while there is not much doubt that the mind operates through the firing of neurons and other brain cells, for the praxeologists the level of analysis starts where one can attribute meaning to human choices. A physiological explanation cannot be the starting point of praxeology, but human purposes and plans can. As Mises wrote: "Economics is not about things and tangible material objects; it is about men, their meanings and actions. Goods, commodities, and wealth and all the other notions of conduct are not elements of nature; they are the elements of human meaning and conduct. He who wants to deal with them must not look at the external word; he must search for them in the meaning of acting men." *Human Action*, 1949, p. 92.

learning how to best satisfy the ends sought, or learning that alternative ends are in fact better targets to seek to satisfy.

As a way of illustrating this statement, Kirzner describes the debate that took place between Benedetto Croce and Vilfredo Pareto at the beginning of the 20<sup>th</sup> century. According to Croce human action can only be understood as purposeful. For Pareto on the other hand, what matters is the “result of action” and the nature of action is irrelevant to economics. This view does not recognize the fact of conscious human choice aiming at a perceived goal, which is not found in the sciences of nature and which sets economics apart. The difference between Croce and Pareto lies with the “teleological” element in human affairs, which means that the “usual temporal relation is reversed, the present being ‘caused’ by the goals set up for the future.”<sup>49</sup> Teleology and purposefulness provide the foundation of praxeology.

The economics of agent omniscience does a poor job of grappling with the human condition of choice in an uncertain and changing world. Coordination in a world of automatons is effortless and the institutional environment within which choices are actually made is insignificant. The role of organizations, money, morals, expectations, etc., is brushed aside. An economics so conceived cannot possibly explain how in coping with our ignorance alternative institutional environments either promote or hinder the coordination of economic activities through time. To understand the real world and the regularities of the market economy, the purposive activity of individuals must be placed in a context in which their cognitive skills are neither super human nor non-existent, and the market process is seen as unfolding in time and within a specific institutional context. In such a view, purposive human beings will learn, adjust and adapt their behavior to better satisfy their ends—whatever those ends may in fact be.

The neoclassical conception of rationality is not grounded in the reality of human action but in a definition that imposes an external benchmark on human behavior. As Kirzner explains, there is no reason to put human behavior in the strait-jacket of neoclassical rationality. The empirical regularities of market phenomena can be explained with a theory resting on purpose, subjectivism, and economizing. They are independent from the existence of limited human cognitive abilities. As Kirzner would later state this basic principle—all that economics requires is that people are alert to that which is in their interest to be alert to. Thus, the essential entrepreneurial element of human action follows directly from the implication for economic understanding that people act purposively to realize a variety of ends, and in so doing they will attempt to arrange means as effectively as possible to realize those ends that they seek.

## **VI. Conclusion**

Kirzner’s achievement in *The Economic Point of View* is to illuminate how the praxeological position emerged in the slow but continuous development of economic science since the end of the 18<sup>th</sup> century. Purposefulness (teleology), subjectivism, and

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<sup>49</sup> Kirzner, p. 164.

rationality (economizing) are the three pillars of the praxeological approach. Kirzner's historical account of the evolution of economic science shed light both on the nature of economic science and on its object.

We emphasize four crucial aspects of Kirzner's work in this introduction:

- the context (historical and intellectual) in which the book was published
- the importance of the subjectivist stance in the building of an objective economic science
- the importance of Kirzner's early position with regard to his future intellectual developments
- the relevance of Kirzner's view in the recent development of behavioral economics and other related approaches

The growth of alternative views to the neoclassical paradigm in the recent times is proof of a growing dissatisfaction among academics of its utility. Behavioral economics offers a different view of the idea of market clearing and social order as shown in economics textbooks. This is where the biggest threat to economics as the science of spontaneous order comes from. The most powerful and most underrated response to this alternative view comes from the development of economics as a science solidly established into the subjectivist approach. A world of automatons is clearly not what economics should strive to describe. But neither should economics only focus on cognitive flaws to the detriment of the element in human action that enables us to explain the emergence of regularities in social phenomena. Kirzner's view truly occupies the middle ground between neoclassical, Shackleian, and behavioral approaches to human action.

In retrospect, Kirzner's first book foreshadows the great economist that he came to be. It establishes the foundations of his future work on the role of the entrepreneurial function, the theory of the market process, and the role of capital. Kirzner is a subtle and committed scholar who is essentialist in explanation, and clear and precise in writing style.