

METHODOLOGICAL INDIVIDUALISM IN CARL MENGER: AN EVALUATION*

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Abstract:

Although Carl Menger, the founder of the Austrian school of economics, is known as a leading figure in the "marginal revolution," his views on the methodology of economics deserve even more attention. In particular, the two very foundations of the Austrian school, namely subjectivism and methodological individualism, directly come from Menger. In this paper, after briefly pointing out the subjectivist elements in Menger's economic analysis, I examine Menger's views on the methodology of economics, which takes methodological individualism as the main basis, and evaluate both his version of individualism and one of the attempts, made by Ludwig Lachmann, to provide rigorous foundations to Menger's arguments. It is argued in this paper that both of these versions exhibit the same inconsistency between methodological individualism and the hypothesis of unintended consequences of intentional human behavior, which has generally been used as an argument in favor of the methodological individualistic social theory.

Özet:

CARL MENGER'de METODOLOJİK BİREYCİLİK: BİR DEĞERLENDİRME

Avusturya iktisadi okulunun kurucusu olan Carl Menger "marjinal devrimin" önde gelen isimlerinden birisi olarak bilinse de, onun iktisat metodolojisine ilişkin görüşlerinin çok daha ilginç olduğu söylenebilir. Özellikle, Avusturya okulunun iki temel unsuru olan sübjektivizm ve metodolojik bireycilik Menger'in temel katkılarından. Bu çalışmada öncelikle Menger'in analizindeki sübjektif unsurlara değinilmekte ve onun iktisat metodolojisine ilişkin görüşleri irdelenmektedir. Bu bakımdan metodolojik bireycilik, Menger'in kendi yaklaşımının temelini oluşturduğundan, özel bir önem taşımaktadır. Bunun yanında, Menger'in yaklaşımına sağlam analitik temeller kazandırma amacıyla olan Ludwig Lachmann'ın bireycilik konusundaki görüşleri de incelenmektedir. Çalışmada, gerek Menger'in ve gerekse Lachmann'ın görüşlerinin aynı güçlükten, yani metodolojik bireycilik ile insanların özgür iradelerine dayanan "istendik davranışlarının istenmedik sonuçları" hipotezi arasındaki tutarsızlıktan kurtulamadıkları öne sürülmektedir.

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Anahtar Sözcükler: Carl Menger, Metodolojik bireycilik, Avusturya İktisat Okulu, kesin bilim, Ludwig Lachmann, yorumsamacılık, istendik davranışın istenmedik sonuçları.

Introduction

One of the distinguishing characteristics of the Austrian school of economics is its emphasis on the methodological foundations of economics and the social sciences in general. Although there are significant differences in the views of different Austrian economists concerning the methodology of economics, the two very foundations of the Austrian school have always been subjectivism and methodological individualism, and these two foundations directly come from Carl Menger, the founder of the Austrian school.

As is well known, Menger's significance in the history of economic analysis lies in his introduction, together with Jevons and Walras, of the idea of marginal utility, in his *Principle of Economics*, published in 1871 (Menger 1981), though he never used this term. In this book, he conceptualized the operation of a market system as governed by subjective valuations of individuals which determine the entire structure of production and allocation of resources and the corresponding enumerations of scarce resources (Kirzner 1990: 103). That is, methodologically speaking, the *Principle* is founded on a subjectivist framework. Another significant aspect of Menger's views is that they rest almost exclusively on methodological individualism, developed especially in his *Investigations into Method*, a book published in 1883 (Menger 1985).

The main focus of this paper is thus methodological: in the first section. After briefly pointing out the subjectivist elements in Menger's economic analysis, I concentrate on his views on the methodology of the "exact" science of economics, which is clearly founded upon methodological individualism. In the second section, I compare and criticize two different perspectives on social theory, or two different versions of methodological individualism within the Austrian school, namely, Menger's version, and Ludwig Lachmann's version which adopts an hermeneutic framework. It is the argument of this paper that both of these versions suffer from the same problem: The tension, if not contradiction, between methodological individualism and the hypothesis of unintended consequences of intentional human behavior, even though this hypothesis has been used in both Menger and the other Austrians as an argument for the methodological individualistic position.

1. Subjectivism and Methodological Individualism In Menger's Writings

1.1. Subjectivism and Economic Analysis

According to Wicksell, "since Ricardo's *Principles*, there has been no book—not even excepting Jevon's brilliant if rather aphoristic achievement and Walras' unfortunately difficult work—which has exercised such great influence on the development of economics as Menger's *Grundsätze*." (quoted by Hayek 1981: 21)

In the Preface of this book, Menger asserts that economic theory is concerned with the satisfaction of material needs of individuals. For him, “economic theory is concerned, not with particular rules for economic *activity*, but the *conditions* under which men engage in provident activity directed to the satisfaction of their needs.” (Menger 1981: 48)

The needs of individuals are, of course, satisfied by goods. If a thing is to become a good, four prerequisites must be present simultaneously: A human need, the capability of that thing to satisfy this need, human knowledge of this “causal connection” between that thing and satisfaction of this need, and finally, sufficient amount of that thing for the satisfaction of the need: “...from this it is evident that goods-character is nothing inherent in goods and not a property of goods, but merely a relationship between certain things and men, the things obviously ceasing to be goods with the disappearance of this relationship” (Menger 1981: 52).

In this respect, there is no essential difference between consumer goods, or in Menger’s terms “goods of first order,” and production goods, being “goods of higher order,” including land and labor services, because both kinds of goods possess the causal connection between things and the satisfaction of needs. The only difference between them is that “goods of first order have a direct and goods of second order an indirect causal relation with the satisfaction of our needs.” (Menger 1981: 57) According to one interpreter (Garrison 1990: 135), this difference can be attributed to the time element involved in production process. Higher order goods are transformed sequentially into goods of lower and lower order until they emerge as consumer goods. For example, some of these higher order goods, such as seed grain, which could be used for immediate consumption, become capital goods if they are used in the production process. In other words, capital goods arise as an outcome of the time preference; the choice between the satisfaction of the needs at present or in a more distant time period (Menger 1981: 155)¹.

On the other hand, the *economic* character of goods arises from the “quantitative relationship” between the needs and the available quantity of that good. If the “requirements” for goods are larger than the available quantities of those goods, some of the needs will remain unsatisfied, and therefore, a choice between needs with respect to their importance must be made, and furthermore, in this choice one must try “to obtain the greatest possible result with a given quantity of the good or a given result with the smallest possible quantity” (Menger 1981: 95-96). These kinds of goods will be “economic” goods; others, the goods whose available quantities are greater or equal to the requirements for them, are “noneconomic” goods (Menger 1981: 97). The exchange value of an “economic” good is determined by this relationship between requirements for and available quantities of goods. The most important principle in the determination of value is marginal utility, which illuminates a “difficult and previously unexplored field of

psychology" (Menger 1981: 128). On this conception, equilibrium ("economic") prices of consumer goods are determined by supply and demand, which in turn are determined by utility; that is, by the equality of respective marginal utilities of the goods in question². On the other hand, the prices of production goods, goods of higher order, "is always and without exception determined by the prospective value of the goods of lower order in whose production they serve" (Menger 1981: 150; quoted in Hunt 1992: 320). The prices of production goods are determined, again, by their utilities, which ultimately govern the supply of and the demand for them. In other words value, which "does not exist outside the consciousness of men" (Menger 1981: 121), is entirely a subjective phenomenon. Value is "nothing inherent in goods, no property of them, but merely the importance that we first attribute to the satisfaction of our needs, that is, to our lives and well-being, and in consequence carry over to economic goods as the exclusive causes of the satisfaction of our needs" (Menger 1981: 116).³

It can be inferred from this presentation that the most significant aspect of Menger's economic views is not the idea of marginal utility *per se*, but the foundation of this idea, namely, subjectivism. Nonetheless, such a subjectivism, still widespread in the contemporary neoclassical economics, as a rule couples with the view known as methodological individualism. This is particularly true for Menger. According to Streissler (1990: 60), for example, almost the whole of the "protoneoclassical" strain of German economics at the day had a subjective value theory. Menger's contribution was to develop a new variant of subjective value theory which is founded on methodological individualism. For this reason, I now want to turn to Menger's arguments as to the appropriate methodology of economics, and social science in general, which require methodological individualism as the main basis.

1.2. On The Methodology of Exact Science

In his later book, *Investigations into the Method*, Menger aims at developing a consistent methodology of social sciences. This book is in fact a polemic against the "German Historical School" which had exerted a great influence on the social scientific discourse in Germany at the day, even though his *Principles*, was dedicated, somewhat ironically to Wilhelm Roscher, a leading member of this school.⁴ Menger starts his *Investigation*, with a distinction between two kinds of scientific knowledge or two "orientations of research": the *individual* orientation, dealing with the concrete aspects of the phenomena, and the *general* orientation, aiming at cognition of the general character of the phenomena in question (Menger 1985: 35). However, here, the word individual as opposed to general must not be confused with "singular" as opposed to "collective." For example,

A definite nation, a definite state, a concrete economy, an association, a community, etc., are examples of individual phenomena, but by no means of singular phenomena (but of collective phenomena instead); whereas the phenomenal forms of the commodity, of the use value, of the entrepreneur, etc., are indeed general, but not collective phenomena. (Menger 1985: 37 n).

This distinction between individual and general is essential in distinguishing the "historical" sciences from the "theoretical" or "exact" sciences. In this regard, there are three groups of sciences in the field of economy: 1) Historical sciences, "which have the task of investigating and describing the individual nature and the individual connection of economic phenomena"; 2) "theoretical economics, with the task of investigating and describing their general nature and general connection (their laws)"; 3) practical sciences of national economy, "with the task of investigating and describing the basic principles for suitable action (adapted to the variety of conditions) in the field of national economy (economic policy and the science of finance)." (Menger 1985: 38-39) In this sense, economics is a theoretical or exact science which "has the task of investigating the *general nature* and the *general connection* of economic phenomena, not of analyzing economic *concepts* and of drawing the logical conclusions resulting from this analysis." (Menger 1985: 37, n.4)

With respect to empirical phenomena within the general sphere, we must distinguish between empirical *types*, such as "the phenomena of purchase, of money, of supply and demand, of price, of capital, of rate of interest", and the relationships between different types, which is called *typical* relationships, such as "the regular drop in price of a commodity as a result of the increase in supply, the rise in price of a commodity as a result of the increase in currency, the lowering the rate of interest as result of considerable accumulation of capital etc." (Menger 1985: 36). These typical relationships designate "laws" in economic sciences, which illuminate the "essence" or "nature" of these phenomena:

Without cognition of the typical relationship we would be deprived not only of a deeper understanding of the real world, ... but also, as may easily be seen, of all cognition extending beyond immediate observation, i.e., of any *prediction* and *control* of things. All human prediction and, indirectly, all arbitrary shaping of things is conditioned by that knowledge which we previously have called *general*. (Menger 1985: 36)

According to Hutchison (1973: 17-18), two points are important in this distinction between the general and the individual orientation. First, general knowledge is concerned with "prediction and control"; and second, Menger's conception of economic theory seems to be an "essentialist" position, a view,

according to Popper, that “scientific research must penetrate into the essence of things in order to explain them” (quoted by Hutchison 1973: 18). But even though he may be a methodological essentialist, Menger should not be characterized as an “instrumentalist”, because, as both the above and the following passages show, he emphasizes “a deeper understanding” of the nature of the phenomena, “the real world,” before making any predictions!⁵

The purpose of the theoretical sciences is understanding of the real world, knowledge of it extending beyond immediate experience, and control of it. We understand phenomena by means of theories as we become aware of them in each concrete case merely as exemplifications of a general regularity. We attain a knowledge of phenomena extending beyond immediate experience by drawing conclusions, in the concrete case, from certain observed facts about other facts not immediately perceived.... We control the real world in that, on the basis of our theoretical knowledge, we set the conditions of a phenomenon which are within our control, and are able, in such a way to produce the phenomenon itself. (Menger 1985: 56)

The types and the typical relationships (the laws) of the world of phenomena can be divided into two parts; those regularities without any exception (“*laws of nature*”), and those regularities in which exceptions are possible (“*empirical laws*”) (Menger 1985: 50). However, this is not to say that the “laws of nature” can only be observed in nature whereas to social phenomena only “empirical laws” apply, because “the number of natural sciences which absolutely comprise strict laws of nature is also small, and the value of those which show only empirical laws is nevertheless beyond question” (Menger 1985:52). Even more importantly, especially regarding economics, he believes that “whatever the degree of strictness of the laws characteristics of the realm of social phenomena may be, ... the character of economics as a *theoretical* science is by no means affected” (Menger 1985: 51), for

the *theory* of economy must in no case be confused with the *historical* sciences of economy, or with the *practical* ones. Only the person who is completely in the dark about the formal nature and the problems of theoretical economics could perceive in it a *historical* science because the general (theoretical) knowledge which it embraces ostensibly, or really, shows less strictness than in the natural sciences. (Menger 1985: 51)

According to Menger, the degree of the strictness of laws is significant only from the point of view of understanding, and predicting and controlling the phenomena, because “the greater the strictness of the laws, the greater also the degree of certainty which, on the basis of the laws, conclusions can be drawn

beyond direct experience about the occurrence of future phenomena, or about the coexistence of simultaneous phenomena not directly observed.” (Menger 1985: 52) Still, “all these differences, ... are, in respect to the prediction and control of phenomena, differences in degree, not in principle” (Menger 1985: 52). Thus, the correct contrast under discussion should be between “empirical” and the “*exact*” laws, and not between empirical laws and the laws of nature. In this regard, the aim of the “exact” orientation

is the determination of strict laws of phenomena, of regularities in the succession of phenomena which do not present themselves to us as absolute, but which in respect to the approaches to cognition by which we attain to them simply bear within themselves the guarantee of absoluteness. (Menger 1985: 59)

Based on this distinction, he maintains that “there are natural sciences which are not exact ones (e.g., physiology, meteorology), and, conversely, there are exact sciences which are not natural sciences (e.g., pure economics)” (Menger 1985: 59n). The laws of theoretical economics are “*exact laws of the ethical world*” (p. 59n), that is, theoretical economics is “an *exact ethical science*” (p. 60n). However, here the term ethical should not be taken to imply that economics cannot be free from value judgments. Such an argument, according to Menger, simply contradicts the nature of the exact orientation of theoretical research (Menger 1985: 236), even a practical science of economy must be free from moral judgments, for otherwise such an enterprise can never be anything more than moral writings about economy. Thus, “the so-called ‘ethical orientation’ of political economy is ... a vague postulate devoid of any deeper meaning, ... a confusion of thought” (Menger 1985: 237, quoted in Hunt 1992: 323-24).

On the other hand, regarding the epistemological status of exact laws which can be verified both by experience and “laws of thinking,” we have one “rule of cognition” (Menger 1985: 60) such that:

whatever was observed in even only one case must always put in an appearance again under exactly the same actual conditions; or, what is in essence the same thing, that strictly typical phenomena of a definite kind must always, and indeed in consideration of our laws of thinking, simply of necessity, be followed by strictly typical phenomena of just as definite and different a type. Phenomena A and B must under the same conditions always be followed by the strictly typical phenomenon C in so far as A and B are thought of as strictly typical and the succession of phenomena under discussion here has been observed even in only a single case. This rule holds true not only of the nature of phenomena, but also of their measure, and experience not only offers us no exception to it, but such a thing simply seems inconceivable to the critical mind.

A second rule is that “a circumstance which was recognized as irrelevant only in one case in respect to the succession of phenomena will always and of necessity prove to be irrelevant under precisely the same actual conditions in respect to the same result.” (Menger 1985: 60) Although such a conception implies an empiricist epistemology,⁶ according to Menger the knowledge of exact laws are not attainable through an “empirical-realistic orientation” like that of Bacon. That is to say, the propositions of an exact science are not, in Popper’s language, “falsifiable.” For Menger, testing the pure theory of economy by sense experience is “analogous to that of the mathematician who wants to correct the principles of geometry by measuring real objects, without reflecting that the latter are indeed not identical with the magnitudes which pure geometry presumes or that every measurement of necessity implies elements of inexactitude” (Menger 1985: 70). Likewise, natural sciences, like chemistry, “does not teach us ‘real concepts’ of definite groups of concrete phenomena. Its elements and compounds are, rather, unempirical in their complete purity, they are not to be observed in nature uninfluenced by human art; indeed, to some extent, they cannot be prepared synthetically” (Menger 1985: 85). Then, the knowledge of exact laws can only be attained through examining these constitutive elements and compounds “in their complete purity” which in turn requires a methodological individualist position, as we are about to see.

1.3. Methodological Individualism and Unintended Consequences

According to Menger, the correct method in an exact science is to try “to ascertain the *simplest elements* of everything real, elements which must be thought of as strictly typical just because they are the simplest” (Menger 1985: 60). With respect to the “laws” of phenomena the same is true: Exact science examines “how more complicated phenomena develop from the simplest, in part even unempirical elements of the real world in their (likewise unempirical) isolation from all other influences, with constant consideration of exact (likewise ideal!) measure” (Menger 1985: 61). That is to say, the correct method of an exact science of economy is methodological individualism, and the nature of exact orientation

consists in the fact that we reduce human phenomena to their most original and simplest constitutive factors. We join to the latter the measure corresponding to their nature, and finally try to investigate the laws by which *more complicated* human phenomena are formed from those simplest elements, thought of their isolation. (Menger 1985: 62)

The simplest unit in economics is the “individual economy”: “By *economy* we understand the precautionary activity of humans directed toward covering their material needs; by *national economy*, the social form of this activity” (Menger 1985: 62). This distinction is defined with reference to exchange relations: If there is no exchange between individuals, the term “national economy,” if permissible in

this case at all, is just the summation of individual economies in a nation. However, when the members of a nation come into “economic communication” with each other, the concept of “national economy” gains a different meaning. Here we cannot even speak of national economy (Menger 1985: 193) since

under our present social conditions the nation is simply not *the* economic subject (nor are its functionaries). The leaders of the individual and common economies are really the economic subjects. The goal of the latter is on the whole not the meeting of the material needs of the nation in its totality, but the meeting of *their* material needs or of those of other definite actual or potential persons. Finally, the economic means at hand do not serve to secure the needs of the nation as a unit, but merely those of actual or potential people. (Menger 1985: 193-194)

Therefore, economics is concerned with the self-interested behavior of individuals. However, the thesis of private interest in the form that “humans truly are guided in their *economic* activity exclusively by consideration of their individual interest” (Menger 1985: 83) is erroneous, because other motives, like “public spirit, love of one’s fellow men, custom, feeling for justice, and other similar factors determine man’s economic actions.” (Menger 1985: 84) Then, it would be fair to claim that “the circumstance that people are not guided exclusively by self-interest prohibits ... the strict regularity of human action in general, and of economic action in particular —and thereby eliminates the possibility of a rigorous economic theory” (Menger 1985: 84). Another factor that prevents strict regularity in human sphere is the existence of *error*: Even if human beings are guided by their self-interests, “in innumerable cases they are in error about their economic interest, or in ignorance of the economic state of affairs” (Menger 1985: 84). That is to say, although economics is an exact science, it

cannot provide understanding of human phenomena in their totality or of a concrete portion thereof, *but* it can provide understanding of *one of the most important sides of human life*. “*The exact theory of political economy*” is a theory of this kind, a theory which teaches us to follow and understand in an exact way the manifestations of human self-interest in the efforts of economic humans aimed at the provision of their material needs. (Menger 1985: 87)

The central concern in economic analysis is therefore self-interested behavior of the individual “economies.” The “national economy,” on the other hand, is merely a result of the innumerable individual economic actions; in order to understand this “fiction,” we must split it into its “true” elements, namely individuals (Menger 1985: 93). Yet, even though the national economy emerges from individual behavior, it is something different:

National economy in the common sense of the word, is *by no means a juxtaposition of isolated individual economies*. The latter, rather, are closely tied together by traffic with one another.... [the economy] is really, on the contrary, a complex, or if one wishes, an *organism of economies* (of singular and common economies), but, we repeat, it is not itself an economy.... It is the same as in a machine which presents a unit made up of wheels, and so on, without being a wheel itself. (Menger 1985: 194)

This issue carries us directly to the problem of “spontaneous order,” to use Friedrich A. Hayek’s term, or “the unintended consequences of intentional behavior.” According to Menger, both the functions and the origins of social structures and institutions can be explained on the basis of an “organicist” analogy between these structures and natural organisms, an analogy which focuses on the relations between the whole and the parts:

The normal function and development of the unit of an organism are thus conditioned by those of its parts; the latter in turn are conditioned by the connection of the parts to form a higher unit; and finally the normal function and the development of each single organ are conditioned by those of the remaining organs.

...
The same is true with respect to the *origin* of a series of social phenomena. Natural organisms almost without exception exhibit, when closely observed, a really admirable functionality of all parts with respect to the whole, a functionality which is not, however, the result of human *calculation*, but of a *natural* process. Similarly, we can observe in numerous social institutions a strikingly apparent functionality with respect to the whole. But with closer consideration they still do not prove to be the result of *intention aimed at this purpose*, i.e., the result of agreement of members of society or of positive legislation. They too, present themselves to us rather as “natural” products (in a certain sense), *as unintended results of historical development*. (Menger 1985: 130)

Therefore, the organicist analogy is somewhat inadequate, because only a part of social phenomena is similar to natural ones. “A large number of social structures are not the result of a natural process.... They are the result of a purposeful activity of humans directed toward their establishment and development (the result of agreement of the members of society or of positive legislation)” (Menger 1985: 131). Secondly, whereas natural organisms function in a mechanical way, the social ‘organisms’ “simply cannot be viewed and interpreted as the product of purely mechanical force effects. They are, rather, the result of human efforts, the efforts of thinking, feeling, acting human beings” (Menger 1985: 133). In other words, “some social phenomena are the results of a *common will* directed toward their establishment (agreement, positive legislation, etc.), while others are unintended result of human efforts aimed at attaining essentially *individual* goals (the unintended results of these)” (Menger 1985: 133).

A perfect example to the unintended consequences of individual self-interested behavior is the origin of money as a medium of exchange. According to Menger (1892), money arises from the fact that there is a difference in magnitude between the price at which one can buy at a given market, and the price at which one is willing to sell the same commodity (Menger 1990: 243). On the basis of this difference, it is possible to define the concept of the *saleability* of a commodity. Goods can be identified as “*more or less saleable*, according to the greater or less facility with which they can be disposed of a market at any convenient time at current purchasing prices, or with less or more diminution of the same...” (Menger 1990: 244). At a given time, some of the existing goods are more desirable to individuals within the market system, that is, effective demand for them is greater than that of others. In this case, any seller in principle will want to exchange these specific goods which are more “saleable” than others with the commodity he or she wishes to sell, even if that seller does not need that commodity for his or her own immediate consumption. Therefore, the most “saleable” commodity will gain a universal acceptance in the markets as a medium of exchange; and as soon as it is accepted as a medium of exchange, its “saleability” will increase cumulatively (Menger 1990: 230). Historically speaking, precious metals have been more or less the most saleable commodities, and therefore they have become money. Besides this, the properties of these metals, such as their low costs of transportation as compared to their value, their unlimited durability, divisibility, homogeneity, and the relatively slight cost of hoarding them have contributed to their becoming a medium of exchange (Menger 1990: 253). This development, according to Menger, has taken place without any state compulsion or voluntary convention of traders. It is purely spontaneous:

Money has not been generated by law. In its origin it is a social, and not a state institution.... On the other hand, however, by state recognition and state regulation, this social institution of money has been perfected and adjusted to the manifold and varying needs of an evolving commerce, just as customary rights have been perfected and adjusted by state law. (Menger 1990: 255)

As can be seen from this example, according to Menger, pure economic theory as an exact science, which aims at understanding the general “nature” of economic phenomena, is specifically concerned with the unintended consequences of purposeful, intentional behavior of individuals. On this conception, scientific analysis must proceed as abstracting the essential features of empirical phenomena, starting from the simplest elements, namely individual economies, and proceeding to more and more complex relations by tracing the unintended consequences of intentional individual action.

As a last word, it is interesting to note that the views on methodology by the members of the contemporary Austrian school is profoundly different from those of Menger. Although all the members defend subjectivism and methodological individualism, in many respects the School has outgrown or rejected Menger's methodological outlook, and it cannot be said that current Austrian methodological views derive predominantly from Carl Menger. For example, the early chapters of von Mises', who defends rationalism as the methodology of Austrian school, *Human Action*, which discusswes methodology, contains no single reference to Menger's *Investigations*. (White 1985: ix). Furthermore, there are some differences between the methodological views of different Austrians, though there is a certain tendency towards rationalist epistemology (Ebeling 1990: 368-370; Kirzner 1976). For example, whereas Böhm-Bawerk defends the "deductive" method, Friedrich von Wieser emphasized the "introspective" source of economic analysis, believing that it gave economics a stronger foundation than those found in the natural sciences. Along the same lines, Ludwig Lachmann, following Max Weber, emphasized the significance of the principle of "understanding" (Verstehen), as a view that leads to the "interpretative" or "hermeneutic" social theory, for he believed that the aim of the analysis is to make the purposeful human activity intelligible. On the other hand, F. A. Hayek emphasized the "unintended consequences" of human behavior, so that social scientists must be careful about making predictions. Yet, the unifying principle for all of them is methodological individualism, which is Menger's outlasting contribution not only to the Austrian school, but also, more generally, to the neoclassical economics.

2. Methodological Individualism and Hermeneutics

2. 1. A Note on Menger's Methodological Individualism

As we have seen, there are two closely related aspects of Menger's views of the methodology of social science; methodological individualism and the idea of unintended consequences of intentional, purposeful human behavior. However, these two aspects must be kept distinct from each other, and there is a certain tension between them. But before proceeding to this discussion, I would firstly like to consider Menger's methodological individualism. For this reason, it would be helpful to consider methodological individualism at a general level.

According to Anthony Giddens (1984: 214), for example, the doctrines that advocate methodological individualism involve one or more of the following theses:

- (1) "Truistic social-atomism": the view which holds, that it is self evident that social phenomena can be explained only in terms of the analysis of the conduct of individuals;
- (2) The idea that all statements about social phenomena can be reduced, without loss of meaning, to descriptions of the qualities of individuals;
- (3) The assertion that only individuals are really implying that any concept which refers to properties of collectivities or social systems are abstract models,

constructions of the theorist, in some way that the notion of “individual” is not; (4) The allegation that there cannot be laws in the social sciences, save in so far as there are laws about the psychological dispositions of individuals.⁷

It is evident that Menger’s position can be characterized as holding all these four propositions. However, with respect to the conduct of the analysis in an “exact” science, we need to distinguish between three related but distinct theses within methodological individualism; to use Little’s (1991:183-188) taxonomy, for such a distinction can reveal the weaknesses in Menger’s arguments concerning (1) *Ontological thesis*: all social entities are reducible without remainder to logical compounds of individuals. Social entities are *nothing but* ensembles of individuals in various relations to one another; (2) *The meaning thesis*: social concepts must be *definable* in terms of concepts that refer only to individuals, and their relations and behavior; (3) *The explanation thesis*: there are no autonomous social explanations; instead all social facts and regularities must ultimately be *explicable* in terms of facts about individuals--their motives, powers, beliefs, and capacities.

The ontological thesis is literally true; society is made up or consists of people. But since this is a truism, it does not yield us interesting insights for an adequate social theory; it can be used to defend any kind of social theory. More importantly, the ontological thesis does not entail the theses about meaning and explanation (Little 1991: 200). The meaning thesis, on the other hand, makes sense if the facts refer only to individuals and their psychological properties. But there is no reason to think that such a reduction is possible. Facts about individuals always make reference to social contexts. The predicates designating properties special to persons all presuppose a social context for their employment: “A tribesman implies a tribe, the cashing of a cheque a banking system” (Bhaskar 1989: 28). Secondly, the facts about individuals, such as the motives of a criminal, are not necessarily either more observable or easier to understand than social facts, such as the procedures of a court; while comparison of the concepts like love and war shows that those properties that apply to individuals are not necessarily either clearer or easier to define than those that designate social phenomena (Bhaskar 1989, p.28).⁸ Considering the explanation thesis, we can assert that there are some *emergent* properties of societies irreducible to the dynamics of individuals. In fact, with respect to explanation, there are two possibilities: (a) Laws might exist among phenomena at the higher level of description that are not derivable from laws at the lower level, and (b) It might be that regularities at the higher level are in fact determined by regularities at the lower level, but pragmatic features of explanation make it preferable *not* to perform the reduction (Little 1991:187). Still, from an ontological point of view, if it is the case that there are some emergent properties in society, or there is a discontinuity between the level of individual and the level of social., then we need another view to explain social processes, irrespective of the pragmatic features of explanation.

Although Menger's whole system rests on methodological individualism, as far as I can see, he has no argument for *methodological* individualism, to be conceived as consisting all these three theses. He, together with almost the whole of the Neoclassical economists, takes the "truistic social atomism" granted, and in fact defends only *ontological* individualism, that is, the thesis that all social *entities* are reducible to logical compounds of individuals, and social *entities* are nothing but ensembles of individuals. Even if a society is just a collection of individuals, the meaning and the explanation theses do not follow from this, as we have just seen. That is to say, Menger confuses between these two distinct levels.⁹ But even more importantly, the ontological thesis itself is not necessarily immune to criticism, if one accepts the claim that societies have some *emergent* properties irreducible to the dynamics of individuals. A society has a different ontological status than those of the individuals that constitute the society (Bhaskar 1989, especially chapter 2). Generally speaking, social structures or relations cannot be explained on the basis of facts about individuals; on the contrary, facts about individuals always make reference to social contexts. Without such a context we cannot even define a specific individual. Nevertheless, it should be stressed, as Giddens (1984: 220) does, upon that while "the methodological individualists are wrong in so far as they claim that social categories can be reduced to descriptions in terms of individual predicates ... they are right to insist that 'social forces' are always nothing more and nothing less than mixes or intended and unintended consequences of action undertaken in specifiable contexts." In this regard, we should bear in mind that Menger's position accommodates the fact that even if human behavior is characterized by intentionality, some social phenomena emerges as unintended consequences of intentional behavior -as we have seen when considering his analysis of money. However, what we call as the "unintended consequences" are nothing but the "emergent" properties of social structures. That is, social structures, relations, etc. arise from intentional behaviors of individuals but they cannot be reduced to these behaviors, the social level must have a different ontological status than its constituents, individual actions. For this reason, it is in principle the case that we cannot explain social phenomena merely on the basis of individuals. In other words, there is a certain tension between Menger's individualism and the idea of the "spontaneous order." It can be argued that Menger was aware of the problem, for he thought of a social entity as a form of "organism" constituted by individual "economies" which "are closely tied together by traffic with one another." Nevertheless, such a conception of "organism", with the idea of "traffic" at its center, which emerges as a result of the unintended consequences, implies that the ontological status of these "organisms" is different from that of the individual behavior. In other words, the level of "organisms" is as real as the level of individual, for these organisms too have the power of "making a

difference,” a shorthand but convenient definition of the concept of “agency.” On this conception, “anything which is capable of bringing about a change in something (including itself) is an agent.” (Bhaskar 1975: 109). That is, the notion of agency implies that in order for something to be an “agent” it must have some “causal power” in the sense that it has the potency “to produce an effect in virtue of its nature, in the absence of constraint and when properly stimulated.” (Harré and Madden 1975: 16).¹⁰ Then it should be clear that Menger’s “organisms” are endowed with causal powers and hence the level of “organisms” must also be incorporated into the scientific endeavor. Despite this, Menger still wishes to found his economic analysis exclusively on methodological individualism. Therefore, in so far as Menger is reluctant to admit the importance of the reality of the “social” level, his “exact” orientation which is concerned with the “essences” of economic phenomena will ultimately fail.

Nevertheless, Menger’s own arguments are not the only ones defending methodological individualism in the Austrian tradition; some Austrian economists, especially Ludwig M. Lachmann, develop arguments using also an hermeneutic framework, whose central category is the idea of “*interpretation*.” Therefore, I would like to turn now to the hermeneutic tradition within the Austrian school.

2. 2. Hermeneutic Social Theory and the Austrian Subjectivism

As is well known, hermeneutics, from the Greek word *hermeneus*, “interpreter,” had arisen as efforts to interpret the Biblical texts. Later it was to become the name of a specific social theory, which asserts that society is essentially conceptual in character, and social life does not exist independently of the concepts about how individuals perceive it. This social theory asserts that social world must be understood from within, rather than explained from without; that is, social science should be concerned with the clarification of meaning and conceptual connections.¹¹ In this regard, the method of social sciences is *conceptual* and their central category is *meaning*, whereas the method of natural sciences is *empirical* and their central category is *causality* (Bhaskar 1989: 134-135; Winch 1958: 95).¹² The aim in social science is not to include human action under a causal law, but to discover the *rules* (or goals or meaning) which guide the action and render it meaningful. And the effort for understanding these rules requires *interpretation*. In other words, hermeneutic approach treats social phenomena as a text to be decoded through imaginative reconstruction of the significance of various elements of the social action (Little 1991: 68). For example, according to Peter Winch, a leading hermeneuticist, social sciences are concerned with meaningful, or “rule following” behavior, and they must be based on the understanding of the rules which constitute the forms under study (Winch 1958:

51-52).¹³ Because of this difference in the social sphere, hermeneuticists, following Max Weber, make a sharp distinction between causal explanation (*erklären*) and “interpretative understanding” (*verstehen*), and thus between science of physical non-human world of nature and the science of the mind, culture, and the history (Winch 1958: 95, 111). Social phenomena can only be rendered intelligible, they cannot be explained in a causal framework. The principle of *verstehen* is both a necessary and sufficient method for the social scientific endeavor (Bhaskar 1989: 135).

Having rejected causal explanation as an appropriate category in social science, hermeneutic theory may proceed along two possible lines (Hollis 1994: 18-19):

(1) *Holistic or “top down”*: The games absorb the players. If actors, at least in their social capacities, desire, believe and therefore do only what is socially expected of them, then they need no separate understanding. If, for instance, they are solely the bearers of social roles, which derive entirely from determinate social positions and dictate all that role-players do, then the method of understanding can proceed exactly as the explanation which would proceed in a pure systems-theory adopting a “structuralist” position.

(2). *Individualist or “bottom up”*: If meanings are subjective first and intersubjective only by mutual accord, an opposite account of understanding is needed. The players construct the games of social life, perhaps in the spirit of the social contract, or of the idea of unintended consequences, often postulated to account for economic, moral, or political order.

Now, if we return to Menger after these brief remarks, some of the above ideas are similar to his views, especially to his emphasis on subjectivism. Menger’s methodological individualism as the method of the exact science of economics requires that the explanation of economic phenomena must be made by rendering those phenomena intelligible in terms of the nature of plans and activities of individuals which give rise to them. If the observation includes subjective or interpretative understanding, Menger’s work can be understood as an hermeneutical attempt (Addleson 1986: 10). Likewise, according to Ludwig Lachmann, if we interpret Menger’s insistence on the “essence” of economic phenomena as the “interpretation of meaning”, we may conclude that Menger defended the possibility of an economic theory designed to interpret meaning (Lavoie 1990: 362). For Lachmann, economics is a social science, that is, it tries to establish systematic generalizations about observable phenomena; and it is a science of human choice which is the manifestation of the free will (Lachmann 1950: 166-167). The free will, or the purposeful human behavior, is the main difference between natural and human sciences. The difference between them does not lie in the differences in material natures of the objects studied, but in the

difference in questions that different sciences ask. Economics can be defined in terms of means and ends. But the means and ends have no material existence; they are simply categories of mind. Therefore, all economic phenomena must be interpreted as manifestations of the human mind, of decisions to seek certain ends with given means. In other words, an economist asks what human choices have caused a given phenomenon. (Lachmann 1950: 168).¹⁴ Therefore, any attempt to explain economic phenomena without any reference to the plans and purposes of individuals will ultimately fail, because such a formalism, as opposed to subjectivism, contradicts the very idea of a social science:

... in the study of the human action we are able to achieve something which must forever remain beyond the purview of the natural sciences, viz. to make events *intelligible* by explaining them in terms of the plans which guide action. (Lachmann 1969: 152)

This is the real meaning of the method of *verstehen*; in studying economics we must ask what consequences are brought about by individuals' plans (Lachmann 1969: 154). This is also an argument about methodological individualism, if a different one from that of Menger's.

Methodological individualism, then, ... means simply that we shall not be satisfied with any type of explanation of social phenomena which does not lead us ultimately to a human plan. This entails that explanations couched in terms of so-called "behavior variables" are not satisfactory explanations of human conduct. (Lachmann 1969: 154)

Such an argument for methodological individualism is analytically more powerful than Menger's own position, for it can recognize the reality and effectiveness of ideas, intentions, and plans in the social sphere, in short the "reconstructed" nature of the social reality and it rests on the notion of human intentionality. Unfortunately, the application of the hermeneutic social theory to the Austrian economics as done by Lachmann also creates important problems. First of all, Lachmann's version of hermeneutics does not seem to be compatible with the main hermeneutic arguments. In Lachmann's views, there is no distinction between interpretation and causal explanation; for example he asserts that a purely formal approach "cannot *explain*, i.e. *make intelligible*, a single human act..." (Lachmann 1950: 169) In this regard, it is interesting to observe that no Austrian seem to be bothered with the difference between explanation and interpretation. Even more curiously, Richard Ebeling (1986: 46) argues that all sciences are human sciences, for all the "facts" are theory laden, that is, they must be interpreted. Although it is correct to say that the "facts" of any science are not only "theory laden" but also "theoretical" in a more radical sense, that is, they are essentially analytical

constructs of the scientist,¹⁵ this does not however entail a hermeneutic position, for the leading hermeneutic argument clearly stresses the method of *verstehen* as the appropriate method only for the social science. The issue here is not simply that of the nature of the scientist's perceptions, but of the nature of the reality itself, no matter how the scientist perceives it. That is to say, in the hermeneutic social theory the emphasis is ontological: the social reality itself is constituted through meaning or rules, and hence it is essentially conceptual.

Another, more serious, problem of this approach is that it does not even question the rational choice model of explanation. However, for most of the hermeneuticists, the rational choice model adopts a particularly "thin" and abstract perspective on agency, emphasizing causal beliefs, material interests and instrumental reasoning (Little 1991: 69). Such a model does not, and cannot, consider the social context in which an intentional behavior occurs. This idea is clearly in contradiction with the hermeneutic social theory. According to Winch, for example, "generally, both the ends sought and the means employed in human life, so far from generating forms of social activity, depend for their very being on those forms" (Winch 1958: 55). That is to say, keeping in mind that the rational choice theory in principle couples with methodological individualism, a hermeneutic position does not necessarily imply methodological individualism. For example, Wilhelm Dilthey, who is regarded as the originator of the hermeneutic social theory, and who adopts a "holistic" view, argued, following Hegel, that the category of "meaning" must be considered as "the category which is peculiar to life and to the historical world." For him, human life can be understood only by means of categories, not applicable to the physical world, like "purpose," "value," and "ideal" as different aspects of "meaning." Dilthey believed that the connectedness of life can be understood only through the meaning that individual parts have for understanding the whole. But what we call "the whole" is in fact internal to the whole of humanity. "Life does not mean anything other than itself. There is nothing in which points to a meaning beyond it" (quoted in Hollis 1994: 17). Again, according to Charles Taylor, one of the leading hermeneuticists, what the atomistic view of human beings

hides from the view, is the way in which an individual is constituted by the language and culture, which can only be maintained and renewed in the communities he is a part of. The community is not simply an aggregation of the individuals; nor is there simply a causal interaction between the two. The community is also constitutive of the individual, in the sense that the self-interpretations which define him are drawn from the interchange which the community carries on. A human being alone is an impossibility, not just *de facto*, but as it were *de iure*.... On our own, as Aristotle says, we would be either beasts or Gods (Taylor 1985a: 8).

Another problematic aspect of the “Austrian hermeneutics” is its belief that human action cannot be predicted and controlled, whereas prediction and control is the central category in natural sciences (Lachmann 1950: 171). The main difficulty of this view, quite apart from the fact that it adopts a positivist conception of science for the natural sciences, is that it does not seem to be compatible, again, with the idea of the unintended consequences. As Kirzner (1976: 48-50) correctly points out, the unpredictability of human knowledge and hence human action is inconsistent with the requirement that economic explanations trace the unintended consequences of human action (Kirzner 1976: 50). In regard to the unintended consequences, the relevant question seems to be whether it is possible to reach a compromise between holism and individualism in this hermeneutic framework, for the idea of unintended consequences, as we have seen, requires a “holistic” or “organicist” level as well. Such a compromise would propose that “the rules of the game constrain the players but also enable them to pursue their own ends. The players make their own history, in part by creating their own rules, but they do not do it in conditions entirely of their own choosing. Action may presuppose structure and yet also shape it” (Hollis 1994: 19).¹⁶ But once such a framework is adopted, methodological individualism ceases to become a possible avenue to proceed. In other words, even though it seems possible to see Menger as belonging to the hermeneutic tradition, like Lachmann did, we still have the same problem: both Menger’s and Lachmann’s own versions of methodological individualism fail to solve the problem of intentionality and unintended consequences satisfactorily.

Conclusion

In this paper, I have presented and pointed out to the weaknesses of the methodological individualism of Carl Menger, including the attempt made by Lachmann to provide more rigorous foundations to Menger’s arguments. In this regard, although Menger is one of the most important figures in the Neoclassical framework, to be conceived broadly, for his views about methodology of social sciences are much more sound than those of many contemporary Neoclassical economists, he has an argument only for ontological individualism, which, contrary to his beliefs, does not necessarily imply methodological individualism, and the framework he defends cannot consider the emergent properties of societies and the social context within which intentional behavior is carried out. On the other hand, Lachmann’s argument for individualism seems more powerful than that of Menger, for it adopts a hermeneutic framework which emphasizes intentional human behavior. Nevertheless, such an “Austrian hermeneutics” has been shown to be inconsistent with the main arguments of the hermeneutic social theory. Furthermore, both of Menger’s and Lachmann’s approaches suffer from the same

difficulty, namely, the inconsistency between subjectivism and the idea of the unintended consequences, and the absence of the social context -which is of absolute importance in social sciences because no individual can even be defined without such a context. In this regard, although most Austrians do not like to be equated with the Neoclassical economics, or with the Chicago orthodoxy for that matter, they are no different in their reductionism, i.e. individualism, and the rational choice framework.

Notes:

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- ¹. This interpretation is the point of departure for the later Austrian capital theory. In this regard, interest rate is a payment for this time preference, not for "abstinence" (Menger 1981: 156). Nevertheless, Menger criticizes Böhm-Bawerk's capital theory, which is based on the notion of time preference, as "one of the greatest errors ever committed" (quoted by Garrison 1990: 133). But it seems that what Menger criticizes is not the idea of time preference but the "formalism" of Böhm-Bawerk's theory, in the sense that economic magnitudes can be related to one another without specific reference to plans and actions of individuals, an opposite approach of subjectivism (Garrison 1990: 134).
- ². However, whereas for Menger the equilibrium at which the utility is maximized is characterized by the equality of marginal utilities of different commodities, by Jevons, and in the contemporary Neoclassical economics, the equilibrium condition is the equality between the ratios of marginal utilities to prices.
- ³. As a critique of the labor theory of value, Menger asserts that "the objectification of the value of goods, which is entirely *subjective* in nature, has nevertheless contributed very greatly to confusion about the basic principles of our science" (Menger, 1981: 121). A labor theory of value is an error because "whether a diamond was found accidentally or was obtained from a diamond pit with the employment of a thousand days of labor is completely irrelevant for its value" (Menger 1981:146).
- ⁴. Nevertheless, he is highly critical of the English classical economics of Adam Smith and his followers too, because this tradition "lacks any assured basis, ... even its most elementary problems have found no solution, and ... it is especially an insufficient basis for the practical sciences of national economy, and thus also of practice in this field." (Menger 1985: 27)
- ⁵. In other words, Menger's position should be interpreted as a "realist" one, which is concerned with the real relations ("essences") behind the empirical phenomena. For an argument of this type, and a critique of Menger's realism, see Lawson (1996). Although Lawson believes that there is no essential link between Menger's realism and his individualist position, I argue that Menger's views on the methodology of economics cannot be separated from his individualism. Still, I agree with Lawson that Menger cannot provide a coherent argument for methodological individualism.
- ⁶. Note the similarity between this formulation and John Stuart Mill's famous "canons of induction," namely, the canon of agreement and the canon of difference. For a brief discussion of Mill's canons, see Harré (1985: 38-42). Still, it should be borne in mind that Menger rejects the extreme empiricist

"orientation" of the German Historical school, even though he was anxious to stress that the true contrast between the Austrian and the German Historical schools "is not even remotely characterized as that between an empirical and a rationalist approach or an inductive and deductive one. Both recognise that the necessary basis for the study of real phenomena and their laws is that of experience. Both recognise ... that induction and deduction are closely related, mutually supporting, and complementary means of knowledge" (Hutchison 1973: 35).

⁷. As we can see from these elements, methodological individualism is actually a special case of the view known as "reductionism". Reductionism asserts that (a) it is possible to provide a rigorous specification of a hierarchy of entities, from higher to lower ones, and hence rank any pair of domains, and (b) the entities and laws of higher levels can be reduced to facts about entities and laws at lower levels (Little 1991: 191). In this framework, then, some higher order entities, properties or powers can be defined, explained, or predicted on the basis of some lower order ones.

⁸. In other words, as Giddens rightly argues: "what the 'individual' is, cannot be taken as obvious. The question here is not that of comparing predicates but of specifying what human agents are like" (1984: 220). Without such an account of the notion of agency, methodological individualism does not make much sense. Unfortunately, the methodological individualists, and Menger for sure, fail to provide such an account.

⁹. Behind such a confusion is the view of what Bhaskar calls the *epistemic fallacy*, namely that "statements about being can be reduced or analysed in terms of statements about knowledge; i.e. that ontological questions can always be transposed into epistemological terms" (Bhaskar 1975: 36). Since according to Bhaskar, the questions of ontology must always be kept distinct from the questions of epistemology, such a view that "being can always be analysed in terms of our knowledge of being" (*ibid.*) is a fallacy.

¹⁰. For fuller discussions of the notions of agency, power and nature, see Bhaskar (1975), Bhaskar (1989), and Harré and Madden (1975, especially chapters 6 and 7).

¹¹. The term "meanings" of the actions is an ambiguous term ranging from what is consciously and individually intended to what is communally and often unintendedly significant (Hollis 1994:17).

¹². For a brief introduction to hermeneutical social theory, see (Little 1991, pp. 68-69). One of the best formulations of the hermeneutic social theory is given by Taylor (1985b).

¹³. Winch in fact follows Ludwig Wittgenstein with respect to the definition of "rules." Wittgenstein's *Philosophical Investigations* uses the notion of a "game" in discussing human action. The rules of a game not only regulate how it is played but, more importantly, define or constitute the game itself. Moves in a game have meaning only within the rules, as, for instance, words have meaning only within a language and within practices of communication (Hollis 1994:18). For a critique of Winch's ideas, see Bhaskar (1989: 132-152).

¹⁴. However, here we do not have to seek the psychological causes that lead to particular decisions, but we must be concerned with the logical consequences of these decisions (Lachmann 1950: 173; Lachmann 1969: 155).

¹⁵. One of the main ingredients of the hermeneutical social theory is the assertion that there are no "brute," atomistic facts, existing independent of the observer, in the social science; they are culture-specific. By this account too, Menger's position can be seen as supporting the hermeneutical argument. As can be seen from one of the above quotations, Menger believes that the elements and compounds constituting the exact science are "unempirical in their complete purity, they are not to be observed in nature uninfluenced by human art; indeed, to some extent, they cannot be prepared synthetically" (Menger 1985: 85). Nevertheless, that the "facts" are culture-bound creates an important problem for the Austrian hermeneutics: the existence of relativism, because conceptualizations and meanings of social life vary across cultures in the interpretive framework. But Austrian or in general rational choice framework is not bothered with this problem, because for them human kind is the same at all times and places.

¹⁶. Such a compromise is arguably reached in Anthony Giddens's "structuration theory." For the outlines of this theory, see Giddens (1984).

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