

# **Rothbard on Consumer Sovereignty and His Implicit Rejection of Mises's Economics**

©J. Patrick Gunning  
Visiting Professor of Economics  
Bryant University  
1150 Douglas Pike  
Smithfield, RI 02917

Please send feedback:  
Email: [gunning@nomadpress.com](mailto:gunning@nomadpress.com)

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## Abstract

Ludwig von Mises made *consumer sovereignty* the foundation of his elucidation of market interaction. An exception to consumer sovereignty is the monopoly price, which can be wasteful. Murray Rothbard rejected consumer sovereignty in favor of the concept of *individual sovereignty*. Rothbard proceeded to build his own elucidation of market interaction on the basis of the latter concept. In this theory, monopoly prices are not wasteful. This seemingly minor difference between the two Austrian economists can be traced to a pivotal and crucial difference in fundamental assumptions about the nature and purpose of economics. Mises sought to create a value-free economics based on the assumption that readers accept the view that people benefit from the division of labor and from its further extension. Rothbard sought to create a ethics-based economics, founded on the assumption that the individual is sovereign.

The difference in the goals of the two authors is reflected by a difference in their definitions of private property rights in a pure, unhampered market economy. Mises defined such an economy as containing sufficient private property rights that relevant external effects could not exist. He defined the benefits and harm associated with external effects in terms of the effect on the division of labor. In his pure market economy, every market action benefits others, except for monopoly. Once he had elucidated action under a system of complete private property, he provided the broad outlines of a framework for analyzing a system with incomplete private property rights, although he did not actually do an analysis. He opened the door for future Austrian economists to evaluate arguments that government intervention could correct a deficiency due to incomplete private property rights.

Rothbard defined his unhampered market economy as containing sufficient private property rights so that individual sovereignty is not compromised. In such an economy, property is possessed exclusively by individuals (1) who are rightful owners of the property or (2) who had acquired the thing in question from rightful owners free exchange or gift. Aside from acquiring a thing through exchange or gift a person could be a rightful owner by being its first user and causing it to be produced with his own energy and other things that he possesses. Because a person is free to use his property as he wishes, others cannot be harmed by his decision to not sell at a lower price, regardless of the reason. Rothbard's approach left no room for the evaluation of government policies relating to external effects. An incomplete private property system, for Rothbard, meant that someone had violated the other's individual sovereignty by invading his private property. The remedy for this was simple: return the property to the rightful owner.

The importance of distinguishing between Mises's and Rothbard's economics derives from Rothbard's (sometimes implicit) claims that he meant to clarify and extend Mises's economics. Many students of Austrian economics believe that they can learn Mises's economics by studying Rothbard. This paper shows that Rothbard's claims are wrong and that students cannot learn about Mises's economics by studying Rothbard's theory of the unhampered market economy.

# **Rothbard on Consumer Sovereignty and His Implicit Rejection of Mises's Economics**

There is a wide gulf between the economics espoused by Ludwig von Mises and that of Murray Rothbard. Evidence of this is Rothbard's rejection of the two pillars upon which Mises's economics is founded. The first is Mises's decision to address his economics to people who accept the classical economists' principle of the harmony of rightly understood interests. The second is the connection Mises established between economics and praxeology via the procedure he recommended for tracing all economic phenomena back to the category of action. An integral part of this procedure was the principle of consumer sovereignty.

Mises repackaged the harmony principle of the classical economists' by employing a concept of the entrepreneur that was invented by Herbert Davenport and promoted by Frank Knight. Using this concept, he rewrote W. H. Hutt's idea of consumer sovereignty in such a way that the entrepreneur function represents all of the want-satisfying action in the pure market economy. He thereby transformed the classical harmony principle into the principle of consumer sovereignty while, at the same time, linking economics to the want-satisfying aspect of action in general.

In his 1960 book, Rothbard criticized Hutt's consumer sovereignty and, in early letters to his publisher, expressed his disapproval of Mises's use of the consumer sovereignty concept. To make this criticism, Rothbard had to dig a deep divide between his own economics and that of Mises. In light of this, it is ironic that he claimed that he was merely popularizing and slightly tweaking Mises. The claim turns out to be false.

The importance to the student of Austrian economics of distinguishing between Mises and Rothbard cannot be exaggerated. On the basis of Rothbard's proposals prior to writing his *Man, Economy and State* (1960 [2004]) and also of Mises's endorsement of the project, an uninformed reader is inclined to believe

that Rothbard's book is a textbook version of Mises's *Human Action*.<sup>1</sup> This belief is likely to be fortified by the fact that the structure of Rothbard's book and of the economics part of Mises's book are similar. Both begin with many chapters on the "pure" or "unhampered" market economy. They are followed by an analysis of economies containing various forms of government intervention.<sup>2</sup> However, in this case, appearances are highly deceiving. It will be shown in this chapter that Mises's pure market economy is very different from Rothbard's unhampered market economy and that this difference portends a fundamental and irreconcilable difference between the two approaches to market interaction. The reason for Rothbard's rejection of consumer sovereignty can be traced directly to the different economics that the two writers advocated.

Part 1 of the essay summarizes Mises's treatment of the subject, including the kinds of interventionist arguments that he believed the consumer sovereignty concept would help economists evaluate. The summary is customized to emphasize differences between Mises and Rothbard. Part 2 describes Rothbard's view of consumer sovereignty, along with his critique of Hutt on the subject. Part 3 compares Mises and Rothbard on their purpose of economics and treatment of policy toward external effects. I conclude that one cannot learn very much about Mises's economics by studying the economics of Rothbard. Part 4 presents a brief conclusion.

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<sup>1</sup>See, for example, Rothbard's statement prior to completing his treatise that "[t]he aim I set myself was to fulfill the essence of Mises's structure of praxiology by spelling it out, step by step, in one coherent, integrated structure" (2004: xxxiv). See also: "The purpose of his treatise was to 'isolate the economic, fill in the interstices, and spell out the detailed implications, as I see them, of the Misesian structure'" (*ibid.*: lxxiv).

<sup>2</sup>It is also necessary to mention the fact that the Mises Institute has hindered the ordinary reader's effort to compare Rothbard and Mises by combining *Man, Economy and State* with Rothbard's more anarchistic and radical book *Power and Market*, thus making the suggestion, if implicit, that Mises may have endorsed Rothbard's broader project. This decision was apparently made because Rothbard himself originally wanted these books published together as a single whole (*ibid.*: lxiv-lxx). *Power and Market* basically presents the extension that Rothbard presumably had in the back of his mind all along – the notion that anarchy can provide a framework for the emergence of his concept of an unhampered market economy in the real world. It can lead to the transformation of an imaginary construction (see below) into a reality.

It is important to realize that Mises regarded government as necessary and anarchy as an impossible framework for the market economy. One who reads Joseph Stromberg's introduction to the 2004 edition cannot help but see that Rothbard was cognizant of this difference with Mises. Frank Meyer, a reviewer of Rothbard's manuscript apparently also saw the sharp break. Yet, Stromberg's discussion of the Mises Institute's publishing the two Rothbard works together does not acknowledge this sharp break in a context that would lead the reader to consider the possibility that Rothbard's book and Mises's treatise are in opposition. He thereby makes it difficult for the reader to recognize the irony of the publication in light of the name of the institute. See *ibid.*: lxxi-iv.

## 1. MISES ON CONSUMER SOVEREIGNTY

Mises presented his economics in his treatise *Human Action* (1966). It was based on the purpose of evaluating arguments for and against economic intervention *that are made by utilitarians who understand the potential utilitarian benefits achievable through a division of labor*. That this fact has not previously been appreciated is largely the result of Mises's convoluted way of presenting it. Instead of presenting it directly at the outset of his studies, he waits until after he has developed his economic theorems about market interaction under the conditions of the pure market economy. Moreover, when he does discuss it, he uses definitions and theorems in the discussion that he had established elsewhere in the treatise but which the typical reader is unlikely to link to an economic theorem.

In spite of his confusing presentation, a student of Mises cannot afford to ignore the logic of his chapter in *Human Action* on the "Harmony and Conflict of Interests." The logic goes something like this. Mises points out that friendly relations among human beings are only possible because of the higher productivity of the division of labor. In a market economy,

[c]ataclysmic competition is substituted for biological competition. [This] "makes for harmony of the interests of all members of society. The very condition from which the irreconcilable conflicts of biological competition arise – viz., the fact that all people by and large strive after the same things – is transformed into a factor making for harmony of interests (*ibid.*: 673).

When the classical economists recognized and stated this observation,

they were trying to stress two points: First, that everybody is interested in the preservation of the social division of labor, the system that multiplies the productivity of human efforts. Second, that in the market society consumers' demand ultimately directs all production activities (*ibid.*: 674).

But "consumer sovereignty is not perfect" (*ibid.*: 681). "[I]n some instances of minor importance, even in the unhampered market economy, monopoly prices may appear" (*ibid.*: 682). "With regard to monopoly prices there is not harmony, but conflict of interests" (*ibid.*: 680).

After appreciating the logic of the principle of the harmony of rightly understood interests (henceforth referred to as PHRUI), the student of Mises must relate it to the goals that he aimed to achieve in his book. An important goal is the evaluation of arguments favoring intervention, or interventionist arguments.<sup>3</sup> Because everyone agrees with the principle of the greater productivity of the division of labor, it is sensible to evaluate interventionist arguments – what Mises variously calls the social or economic “problems” – using this criterion:

The higher productivity of cooperation under division of labor makes society the foremost means of every individual for the attainment of his own ends whatever they may be. The maintenance and further intensification of social cooperation become a concern of everybody. Every world view and every ideology which is not entirely and unconditionally committed to the practice of asceticism and to a life in anchoritic reclusion must pay heed to the fact that society is the great means for the attainment of earthly ends. But then a common ground is won to clear the way for an agreement concerning minor *social problems* and the details of society's organization. However various ideologies may conflict with one another, they harmonize in one point, in the acknowledgment of life in society (*ibid.*: 179, italics added).

Praxeology and economics do not say that men should peacefully cooperate within the frame of societal bonds; they merely say that men must act this way if they want to make their actions attain the ends [they seek to attain] (*ibid.*: 883), Also see *ibid.*: 140.

If the economist directs his evaluations of interventionist policies at the people who already accept the PHRUI, value freedom is achievable. Indeed, it is achievable regardless of the criterion one uses to support an interventionist argument:

Economics...is perfectly neutral with regard to the labor-union doctrine, the credit-expansion doctrine and all such doctrines...Economics does not say labor unionism is a bad myth. It merely says it is an inappropriate means of raising wage rates for all those eager to earn wages. It leaves it to every man to decide whether the realization of the labor-union myth is more important than the avoidance of the inevitable consequences of labor-union policies.

In this sense we may say that economics is apolitical or nonpolitical, although it is the foundation of politics and of every kind of political action. We may furthermore say that it is perfectly neutral with regard to all judgments of value, as it refers always to means and never to the choice of ultimate ends (*ibid.*: 884-5).

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<sup>3</sup>Indeed, this may be regarded as Mises's most important goal. See his discussion at *ibid.*: 10, and 884-885. Also see his discussion of how he was able to achieve value freedom in his *Notes and Recollections* (Mises 1978a: 114).

## The Pure Market Economy

To evaluate a PHRUI-based interventionist argument, one starts by building an image of a pure market economy. Mises defines the pure market economy as follows.

The imaginary construction of a pure or unhampered market economy assumes that there is division of labor and private ownership (control) of the means of production and that consequently there is market exchange of goods and services. It assumes that the operation of the market is not obstructed by institutional factors. It assumes that the government, the social apparatus of compulsion and coercion, is intent upon preserving the operation of the market system, abstains from hindering its functioning, and protects it against encroachments on the part of other people. The market is free; there is no interference of factors, foreign to the market, with prices, wage rates, and interest rates (Mises 1966: 237-8).

The government plays an integral role in this definition. Mises later writes that “[t]he essential feature of government is the enforcement of its decrees by beating, killing, and imprisoning” (*ibid.*: 719). Its role is to prevent fraud and encroachments on private property rights. The government “limit[s] its activities to the preservation of private ownership of the means of production and its protection against violent or fraudulent encroachments” (*ibid.*: 718).

### *Private Property Rights*

I will show that a major difference between Mises and Rothbard concerns the role of government. To define this role in Mises’s pure market economy, one must first understand what he means by private property rights. The rights that are important consist of *rights to control*. In the economic “notion of ownership and property,” “[o]wnership means full control” (*ibid.*: 682).

The question of whether existing private property rights can be justified is not an important issue for Mises. What is important is the implication that someone has the legal right to control actions that have external effects.

Carried through consistently, the right of property would entitle the proprietor to claim all the advantages which the good's employment may generate on the one hand and would burden him with all the disadvantages resulting from its employment on the other hand (*ibid.*: 655).

He defines external effects as a situation in which “some of the consequences of [a person’s] action are outside of the sphere of the benefits he is entitled to reap and of the drawbacks that are put to his debit” (*ibid.*).

In making these definitions of private property rights and external effects, Mises must be making some assumption that enables him to define advantages, disadvantages, benefits and drawbacks. He does not tell the reader in this section how these would be determined if one were to use the image of the pure market economy to evaluate an interventionist argument. We can presume, however, that he defines these terms with reference to the PHRUI. This is implicit in his definition of the pure market economy. The pure market economy contains a market process which is “the adjustment of the individual actions of the various members of the market society to the requirements of mutual cooperation” (*ibid.*: 258). At the same time, “[s]ociety is concerted action, cooperation...[I]t is division of labor and combination of labor” (*ibid.*: 143).

### *Evolution of Property Rights*

Mises recognizes that, in the real world, private property rights and ownership are the result of a long history of expropriation.

The history of private property can be traced back to a point at which it originated out of acts which were certainly not legal. Virtually every owner is the direct or indirect legal successor of people who acquired ownership either by arbitrary appropriation of ownerless things or by violent spoilation of their predecessor (*ibid.*: 683).

This fact is not relevant to economics, however. The relevant fact is that whoever the current owners are and however they came to be the current owners, they are the mandataries of the consumers:

[I]n an unhampered market society the consumers daily decide anew who should own and how much he should own. The consumers allot control of the means of production to those who know how to use them best for the satisfaction of the most urgent wants of the consumers. Only in a legal and formalistic sense can the owners be considered the successors of appropriators and expropriators. In fact, they are mandataries of the consumers, bound by the operation of the market to serve the consumers best. Under capitalism, private property is the consummation of the self-determination of the consumers (*ibid.*).

*The First Owner and the Contestableness of Private Property Rights*

How is it determined who owns property? In most cases, this is not an issue. There are traditional owners (many of whom acquired their ownership rights through expropriation – see above). But consider the case of a resource that is newly regarded as valuable. No one previously valued the resource. Now, due to a change, such as a change in technology or population, it becomes valuable. Mises gives an example of what he calls “no-man’s property.”

In the early days of human civilization, when soil of a quality not inferior to that of the utilized pieces was still abundant, people did not find any fault with...predatory methods [of appropriating private property rights]. When their effects appeared in a decrease in the net returns, the ploughman abandoned his farm and moved to another place. It was only when a country was more densely settled and unoccupied first class land was no longer available for appropriation, that people began to consider such predatory methods wasteful. At that time they consolidated the institution of private property in land (ibid.: 656).

Mises is not concerned here with how the institution of private property in land was consolidated but one must presume that he recognized that a political decision was involved. Some one or group realized that by preventing those who do not conserve the productive powers of the soil from using it, they could reduce waste and raise the net returns. So they used their power, or the power of the government, to take away what had previously been a right by anyone to use the soil. That Mises saw private property rights as flexible is suggested by his statement about how in some cases, the property laws went too far in the name of protecting “the poor, the wage earners, and the peasants against the wealthy entrepreneurs and capitalists” (ibid.: 656).

It seems to follow that, for Mises, incomplete private property rights may represent the fact that, in the current situation, some rights are contestable. Such contestable rights would be in the process of being resolved in some way.

Mises does not invoke the PHRUI as a means of resolving the issue of who should be regarded as the first owner of a right to control property. He must be assuming, therefore, that in many cases in a real market economy, some arbitrator is either already considering a definite resolution, she is scheduled to hear a complaint, or one of the contesting parties is planning a complaint. In short, according to Mises’s approach

to private property in a real market economy, one may not be certain who the owner is of some existing property. The legal right to control the resource in question is not yet certain. Yet if the property is owned, its exclusive control would benefit consumers, no matter who owned it.

It also follows that Mises believed that if the economist wishes to evaluate interventionist arguments that pertain to cases of incomplete property rights, he must build an image of interaction in which there are external effects. The economist cannot and should not rely on the pure market economy in which there is a complete set of private property rights, since the real world is likely to contain contestable private property rights. Mises himself, however, did not build such an image.

### *Loopholes*

In speaking about the incompleteness of private property rights in the real world, Mises writes that the “laws concerning liability and indemnification for damages caused were and still are in some respects deficient.” The reason, he says, is that legislators left “loopholes.” Sometimes these were intentional but at other times they were not. Mises does not discuss unintentional loopholes. He simply notes that individuals are faced with the problem of external costs.

Whether the proprietor's relief from responsibility for some of the disadvantages resulting from his conduct of affairs is the outcome of a deliberate policy on the part of governments and legislators or whether it is an unintentional effect of the traditional wording of laws, it is at any rate a datum which the actors must take into account. They are faced with the problem of external costs. Then some people choose certain modes of want-satisfaction merely on account of the fact that a part of the costs incurred are debited not to them but to other people (*ibid.*: 656).

He asserts that the situation of “external costs” left by such loopholes “could be removed by a reform of the laws concerning liability for damages inflicted and by rescinding the institutional barriers preventing the full operation of private ownership” (*ibid.*: 658). Again he gives no examples.

For students of Austrian economics seeking guidance on a theory of external effects, Mises's discussion is disappointing. It gives no hint about how to evaluate arguments favoring market intervention in the case

of external effects except to suggest a reform of the laws. However, the fact that his discussion says that laws are flexible and contestable suggests at least the possibility that some other intervention may be more desirable from the point of view of the PHRUI.<sup>4</sup>

### **Consumer Sovereignty and the Monopoly Exception**

The key characteristic of the pure market economy is *consumer sovereignty*. The actions of individuals in the role of the resource suppliers and producers are aimed at maximizing money income (Mises 1966: 271-2). In a pure market economy, income-maximizing actions lead to the satisfaction of consumer wants.<sup>5</sup> An exception is monopoly. In this case, the owner of a resource may be able to maximize income by withholding some of the monopolized resource from being used to produce consumer goods even though the PHRUI-based benefits are greater in terms of money than the sacrifice to the supplier. A seller who also owns many units of a particular resource may have an incentive to withhold some of it (*ibid.*: 360-1). This incentive exists if the present value of the revenue of the resource owner would be higher than if he sold the whole amount that he owns.

The withholding of a resource from the use that most benefits consumers is regarded by Mises as a waste. The waste demonstrates that pricing in a pure market economy may lead consumer sovereignty to be compromised. Consumers' wants would not be satisfied as well as otherwise, as judged in terms of rightly understood interests. Mises did not suggest government intervention to deal with monopoly. Nevertheless, he said that the monopoly price could compromise consumer sovereignty in some cases. In other words,

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<sup>4</sup> For a student who is familiar with the work of Ronald Coase on this issue, it seems as if a footnote on Coase's (1960) work is missing; since Coase approached the evaluation of interventionist arguments in the case of external effects in very much the same way as Mises approached the evaluation of other interventionist arguments. Mises's PHRUI foundation is a means of differentiating the two. However, this seems to be a minor point.

<sup>5</sup> A person may diverge from the goal of maximizing money income in order satisfy her own wants. In doing so, she elevates her own wants as a consumer above those of the consumers whose wants she would otherwise cause to be satisfied. Consumer wants are still satisfied to a greater extent, but the economist must, in this circumstance, balance the consumer wants of the resource-supplier or producer against those who consume goods produced by others.

economic reasoning could not assure that the actions of individuals would lead consumers to be served to the greatest extent, as judged by the PHRUI.

### **Tight Relationship Between the Pure Market Economy, Consumer Sovereignty and the Entrepreneur Function**

We have seen that monopoly is an exception to the rule that individuals in a pure market economy serve the consumers' interests. The entrepreneur function is not. Mises does not actually say this. It is implicit in his use of terms. To understand what I mean by this, one must recognize that the entrepreneur function refers to, equivalently, the "entrepreneur in his entrepreneur capacity" and to "entrepreneurs and capitalists." Regarding the term "entrepreneur capacity," Mises says that the entrepreneur in this capacity "is always subject to the full supremacy of the consumers. But it is different with the owners of vendible goods." That the entrepreneur capacity refers to the entrepreneur function can be inferred from passages earlier in the text, before he even defines the entrepreneur function (*ibid.*: 81, 240). Now consider the phrase "entrepreneurs and capitalists." In the passage at *ibid.*: 81, he refers to the capacity of entrepreneur and capitalist. Although he does not cite pages, this is clearly a reference to the section of Chapter 14, where he attempts to define the entrepreneur function by attempting to "think the imaginary construction of a pure entrepreneur to its ultimate logical consequences" (*ibid.*: 253). The pure entrepreneur is penniless. Since a penniless entrepreneur cannot bear uncertainty, the attempt fails. A financing "capitalist is always also virtually an entrepreneur and speculator" (*ibid.*). Henceforth, whenever he wants to refer to the entrepreneur function, he uses the phrase "entrepreneurs and capitalists." In short, in developing theorems relating to the pure market economy, Mises develops a "tight" definition of the entrepreneur function as a producer and uncertainty bearer, who always is the mandatory of the consumers.

### **The Pure Market Economy and Intervention**

Mises approach to “social problems” – i.e., to the problems concerning market intervention – starts with the assumptions of the conditions of the pure market economy – private ownership of the means of production and a government that protects the “operation of the market” against “encroachments on the part of other people” [which includes fraud]:

Starting from these assumptions economics tries to elucidate the operation of a pure market economy. Only at a later stage, having exhausted everything which can be learned from the study of this imaginary construction, does it turn to the study of the various problems raised by interference with the market on the part of governments and other agencies employing coercion and compulsion...There is, of course, no other way available for the elucidation of a measure limiting the free play of the factors operating on an unhampered market than to study first the state of affairs prevailing under economic freedom (*ibid.*: 238).

He goes on to discuss the issue of value judgments:

It is true that economists have drawn from their investigations the conclusion that the goals which most people, practically even all people, are intent on attaining by toiling and working and by economic policy can best be realized where the free market system is not impeded by government decrees. But this is not a preconceived judgment stemming from an insufficient occupation with the operation of government interference with business. It is, on the contrary, the result of a careful unbiased scrutiny of all aspects of interventionism (*ibid.*).

In the first set of quotations, Mises refers to the arguments favoring or opposing intervention. In the second, he refers indirectly to the use of PHRUI when he writes of “what people are intent on attaining” from their economic policy.

Writing these words in a section entitled “The Pure Market Economy,” Mises is telling his readers why this imaginary construction is a necessary part of economic analysis. And he is telling them that the use of this construction yields knowledge which, when followed by the study of market intervention, enables the economist to do value-free evaluations of interventionist arguments based on the PHRUI.

We only learn later that consumer sovereignty is a necessary characteristics of the entrepreneur function in the pure market economy. At the stage where he introduces the pure market economy, even a careful reader is unlikely to realize that he is incorporating the PHRUI into the very definition of the pure market economy.

Mises also writes that this procedure is “the only one that is fitted to solve the problems involved” and he refers to the classical economists and their epigones (*ibid.*: 238-9). By this means, he is stating the claim that the procedure he is describing is derived from that used by his economist predecessors. He is establishing a link between the economics of the past, which used the PHRUI as a criterion for evaluating arguments, and his own economics.

### **Why Only Arguments Based on the PHRUI?**

Why does Mises assert that the purpose of economics is to evaluate interventionist arguments based on the PHRUI? He gives two answers. The first is that the PHRUI is the criterion used by the classical economists. Economists have traditionally studied economic problems (i.e., the problems associated with arguments favoring intervention) by referring to the PHRUI (*ibid.*: 673-4; 682). Thus Mises aims to keep with tradition. The second answer is that economics is only suited to evaluate ideologies that value “earthly things.”

[W]here earthly things are involved, the natural affinity of all men and the identity of the biological conditions for the preservation of their lives come into play. The higher productivity of cooperation under division of labor makes society the foremost means of every individual for the attainment of his own ends whatever they may be. The maintenance and further intensification of *social cooperation* become a concern of everybody. Every world view and every ideology which is not entirely and unconditionally committed to the practice of asceticism and to a life in anchoritic reclusion must pay heed to the fact that *society* is the great means for the attainment of earthly ends. But then a common ground is won to clear the way for an agreement concerning minor social problems and the details of society's organization. However various ideologies may conflict with one another, they harmonize in one point, in the acknowledgment of *life in society* (*ibid.*: 179-80, italics added).

The full meaning of this statement can only be understood by recognizing what Mises means by “social cooperation” and “society.” These terms have a special meaning. They refer to peoples’ recognition of the gains in labor productivity that result from trade which, in turn, is due to specialization and the division of labor. See *ibid.*: 143-5.

## 2. ROTHBARD ON CONSUMER SOVEREIGNTY

Rothbard criticized Mises's view of consumer sovereignty. His criticism was, in the final analysis, based on his ethical view about how people should interact with one another. The key concept in this view was the ethical principle of *individual sovereignty*. So that is where my discussion must begin.

### Individual Sovereignty and Property

Rothbard defines individual sovereignty as follows:

Rather than “consumers’ sovereignty,” it would be more accurate to state that in the free market there is sovereignty of the individual: the individual is sovereign over his own person and actions and over his own property. This may be termed individual self-sovereignty: the individual is sovereign over his own person and actions and over his own property. To earn a monetary return, the individual producer must satisfy consumer demand, but the extent to which he obeys this expected monetary return, and the extent to which he pursues other, nonmonetary factors, is entirely a matter of his own free choice (Rothbard: 2004: 29).

Since individual sovereignty implies sovereignty over property, a full understanding of the concept in question requires one to understand Rothbard's concept of property in an unhampered market economy. He defines property as something a person owns in an unhampered, or free, market.<sup>6</sup> [T]he goods owned are known as property” (*ibid.*: 92). Further elucidation comes from his discussion of how property is acquired in an unhampered market economy:

- (1) In the first place, *each man has ownership over his own self*, over his will and actions, and the manner in which he will exert his own labor.
- (2) He acquires scarce nature-given factors either by appropriating hitherto unused factors for his own use or by receiving them as a gift from someone else, who in the last analysis must have appropriated them as hitherto unused factors.
- (3) He acquires capital goods or consumers' goods either by mixing his own labor with nature-given factors to produce them or by receiving them as a gift from someone else. As in the previous case, gifts must eventually resolve themselves into some actor's production of the goods by the use of his own labor. Clearly, it will be nature-given factors, capital goods, and *durable* consumers' goods that are likely to be handed down through gifts, since nondurable consumers' goods will probably be quickly consumed.

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<sup>6</sup>See his statement at *ibid.* 84-85, where he defines the unhampered “society” and writes that he is concerned in what follows with the task of “working out the laws of the unhampered market.”

(4) He may exchange any type of factor (labor service, nature-given factor, capital good, consumers' good) for any type of factor (*ibid.*: 92-93).

Knowing that all property has a history, Rothbard means to limit property in the unhampered market economy to that which is acquired in one of these four ways. Next, he condenses the four ways to three. He writes that “gifts and exchanges as a source of property must eventually be resolved into: self-ownership, appropriation of unused nature-given factors, and production of capital and consumers' goods...” Thus, these three are “the ultimate sources of property in a free economic system” (*ibid.*: 93). Finally he writes that “[t]hese are the [only] methods of acquiring goods that obtain on the free market, and they include all but the method of violent or other invasive expropriation of the property of others” (*ibid.*).

#### *An Example of How Property is Acquired*

To better understand this concept of private property, consider his example of radio wave and television images. He writes:

In a free society, ownership of these channels would accrue to individuals just like that of land or animals: the first users obtain the property. The first user, Jones, of the wave length of 1,000 kilocycles, would be the absolute owner of this length for his wave area, and it will be his right to continue using it, to abandon it, to sell it, etc. Anyone else who set up a transmitter on the owner's wave length would be as guilty of invasion of another's property right as a trespasser on someone else's land or a thief of someone else's livestock (*ibid.*: 173).

Similarly,

In a free society, fishing rights to the appropriate areas of oceans would be owned by the first users of those areas and then usable or salable to other individuals. Ownership of areas of water that contain fish is directly analogous to private ownership of areas of land or forests that contain animals to be hunted (*ibid.*: 174).

Rothbard does not discuss the possibility that the first user could not be easily identified, to my knowledge.

*The Ethical Foundation*

This definition of property implies that individual sovereignty for Rothbard is the ethical right to be free from violent or invasive acts relating things that have been acquired by the methods he specifies. We can learn more by exploring the meaning of an invasive act. He defines an invasive action as “any action – violence, theft, or fraud – taking away another’s personal freedom or property without his consent” (*ibid.*: 176). This definition implies that in addition to being free from robbery and theft, an individual in an unhampered market economy also has the right to “personal freedom.” What is this personal freedom? One can only surmise that it is the right to be free in the same way that the isolated actor is free. For Rothbard writes that “[f]reedom is meaningfully definable only as absence of interpersonal restrictions” (*ibid.*: 339-40). What Rothbard has in mind by the unhampered market economy is a system in which individuals can do everything they want except to interfere with the freedom of other individuals to do anything they want. How the rights in such an economy would be enforced is not an issue (*ibid.*: 176).

In short, Rothbard’s economics is about interaction in an environment based on a complex set of assumptions that are derived ultimately from individual sovereignty. In this environment, individuals either *do* acquire property exclusively in the three ways he specifies or that they are compelled by authorities to do so. However, if they are compelled, the compulsion cannot interfere with the natural right of the individual to act as a solitary actor, so long as she does not interfere with the rights of others to act as solitary actors and does not impede others’ rights to the property they have acquired in the specified ways. It will be convenient to refer to the individuals who have acquired property in the ways specified as the *rightful owners*. Then we can say that in Rothbard’s unhampered market economy, all property is owned by *rightful owners*.

### **Implications of the Rothbardian Rights Conditions**

For convenience, I call this complex set of assumptions the conditions that Rothbard sets for interaction “Rothbardian rights conditions.” This seems an appropriate name since these conditions could not exist unless people naturally acted in a way that is consistent with his assumptions. Unlike Mises, Rothbard does not associate the conditions with the kind of market economy that was traditionally assumed in economics. He apparently aims to impose conditions that he personally finds attractive.

#### *No Undisputed Property*

One implication of the Rothbardian rights condition concerns the meaning of private property rights intervention. The absence of undisputed property means that the ownership of private property cannot be acquired through the resolution of a dispute. Rothbard does not discuss competing claims to the same property. He assumes either that such disputes do not occur or that the problem of resolving them is a simple matter. Thus in his unhampered market economy, property cannot have emerged as a consequence of a war over, say, hunting or fishing rights. Nor could it have emerged, in a peaceful society, through negotiation under threat of force or through judicial determination.

### **The Unhampered Market Economy and External Effects**

Rothbard’s assumption that all property is owned by rightful owners leads him away from any discussion (1) of an incomplete private property system that is due to the existence of contestable property or (2) of “no-man’s property” (see above). Accordingly, external effects cannot exist so long as the government performs its function in *enforcing* property rights. Consider the following:

One difficulty often raised against a free society of individual property rights is that it ignores the problem of “external diseconomies” or “external costs.” But cases of “external diseconomy” all turn out to be instances of failure of government – the enforcing agency – adequately to enforce individual property rights. The “blame,” therefore, rests not on the institution of

private property, but on the failure of the government to enforce this property right against various subtle forms of invasion – the failure, e.g., to maintain a free society (*ibid.*: 181-2).<sup>7</sup>

Another example is smoke or, more generally, air pollution:

In so far as the outpouring of smoke by factories pollutes the air and damages the persons and property of others, it is an invasive act. It is equivalent to an act of vandalism and in a truly free society would have been punished after court action brought by the victims. Air pollution, then, is not an example of a defect in a system of absolute property rights, but of failure on the part of the government to preserve property rights. Note that the remedy, in a free society, is not the creation of an administrative State bureau to prescribe regulations for smoke control. The remedy is judicial action to punish and proscribe pollution damage to the person and property of others (*ibid.*: 182).<sup>8</sup>

Thus Rothbard defines the “unhampered market economy” as one in which there is a complete set of property rights. They are complete because an ethical principle associated with the concept of invasion can always be applied to determine who owns a legal right to property and because the government, if one is present, always enforces individual sovereignty.

In what Rothbard calls the unhampered market economy, external effects are not present because people either voluntarily choose not to invade others’ persons or property or they are blocked by the government from doing so. Thus action in the unhampered market economy is always beneficial and never harmful.

Recall that Mises assumed that a pure market economy contains a complete set of private property rights. Then, for the purpose of building economic theorems that apply to reality, he assumed that private property rights were incomplete. Rothbard entertains the notion that private property rights might be incomplete. But if this were to happen, natural rights law could be applied to the situation to determine who should own the

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<sup>7</sup>It is not clear in this passage what he means by the failure to maintain a free society, since he has not previously mentioned a need or want for this. That is, he has not told his readers how the free society could be successfully maintained. It is evident, however, that there can be no other source of external effects, since these are ruled out by definition. Rothbard’s free market assumes that we know who owns property and, therefore, that we can identify with certainty when an invasion occurs. Under this assumption, someone who claims that an action causes an external effect must either be correct or mistaken. Either the actor already has the property right to act and, therefore her act cannot be invasive. Or the actor does not have the property right, in which case she is invading someone else’s property. There can be no uncertainty about this.

<sup>8</sup>I did not see a discussion in Rothbard about “coming to the nuisance.” This would be the case if the factory pollution of the air occurred first and then people moved near the factory. I must assume that in this case, he would assume that any act of violence against the factory owner would be an invasion of his property rights. See Cordato (1992) for an extension of Rothbardian rights conditions to the case of coming to the nuisance.

property in question. Accordingly, there is no point in trying to produce economic theorems. For better or worse according to some other standard, all that needs to be done to transform the hampered market economy into an unhampered one is for the government to enforce private property rights in a way that is in accord with Rothbardian rights conditions. Rothbard does not ask how people might act under a condition of incomplete private property rights. He merely says that such a condition would not accord with the Rothbardian rights conditions. Because of this, invaders are identifiable and should be punished by government coercion or individuals should change their actions. The question of whether history would or would not reveal what the private property rights should be, according to the Rothbardian rights ethic does not occur to him. In other words, he is not concerned with the practical problem of determining private property rights in a real society.

### **Market Intervention and Utility**

In light of the principle of individual sovereignty, it is somewhat surprising that Rothbard describes the market economy and intervention in terms of the conventional term “utility.” What he means by this is typically unclear. For example, he uses the term in the context of making an argument that aims to logically prove the following proposition:

In sum, the free market always benefits every participant, and it maximizes social utility *ex ante*; it also tends to do so *ex post*, for it contains an efficient mechanism for speedily converting anticipations into realizations (Rothbard 1994: 891).

His proof starts with a discussion of *ex ante* utility. He states the proposition that “when the society is free and there is no intervention, everyone will always act in the way that he believes will maximize his utility.” He goes on to discuss exchange: “Any exchange on the free market, indeed any action in the free society, occurs because it is expected to benefit each party concerned. Thus an increase in expected utility is a necessary condition of action in an unhampered market economy” (879). Then he turns to *ex post* utility. An individual may make an error. To deal with error, he considers the entrepreneur, on the one hand, and the

consumer-saver on the other. Since he had not carefully defined these terms previously, this distinction introduces some imprecision into his analysis.

He says that the entrepreneur may err but because his error will result in loss, we need not worry about it. The market takes care of such errors (*ibid.*: 885). He writes that “[p]rofits and losses spur rapid adjustments to *consumer demands*; at the same time, they perform the function of getting money out of the hands of the inefficient entrepreneurs and into the hands of the good ones” (*ibid.*, italics added). This competitive process “insures an ever smoother market adjustment to changes in conditions” (*ibid.*: 886).

It is not easy to reconcile Rothbard’s discussion of entrepreneur errors with the individual sovereignty concept. Basically he shifts from a discussion of the harm to the individual entrepreneur to a discussion of the benefits to consumers. He aims to show that errors are not a problem. However, what he actually does is invoke the principle of consumer utility to offset the assumed decrease in utility to the error-making entrepreneur. Yet, he does not actually say that the benefits to consumers (and perhaps to other entrepreneurs) are greater than the harm to the error-making entrepreneur. So the discussion does not enable him to support the proposition he purports to be trying to prove. Indeed, to support that position, he would have to radically change his criteria for defining benefit, since the principle he seems to invoke in his proof is precisely the one that he had earlier rejected, namely, consumer sovereignty.

Thus, he seems to have performed a sleight of hand. He does something similar in his discussion of the errors of others. The first thing to note is that he fails to consider the saver. The household that saves in financial markets does not face competition. Its saving is like its consumption spending. The household may err in both decisions. Household errors are very different from those that occur in an environment that we might loosely call entrepreneurial competition.<sup>9</sup> It is true that everyone has a propensity to avoid error.

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<sup>9</sup>It is necessary to invoke the “usual” connotation because, unlike Mises, Rothbard does not identify the entrepreneur function or refer to the definition of Mises. We must assume that he does not include the saver as an entrepreneur who is subject to the competitive process he describes. It is true that he uses the term “capitalist-entrepreneur” (*ibid.*: 886). He defines this role in the following way:

However, the environment of competition is quite different from the environment of personal decision-making about saving and consumption spending.

Although he disregards errors by households as savers, he does discuss errors by households as consumers. Again, he performs a sleight of hand. Instead of trying to show that losses due to consumer error are offset by other gains, as he purported to do in the case of the capitalist-entrepreneur, he changes the subject. Because he ultimately aims to evaluate some type of market intervention, he proposes to contrast the errors of households as consumers with the errors of households as voters. The voters, he assumes, are the ultimate decision-makers on whether a particular intervention will be adopted. It follows that if households are likely to make errors in deciding collectively on an intervention, the losses due to the intervention, regardless of what it is, are likely to be greater than the losses to the household from erroneous buying decisions. Although this argument seems reasonable, it is not related to the point that he sets out to prove and that he claims to have been proven.<sup>10</sup>

The only sensible conclusion that one can reach about this departure from pure individual sovereignty into the realm of utility analysis is that it fails to achieve the aim he set out to achieve. He does not prove the proposition. Simply put, the exercise conflates his ethic of individual sovereignty with utility.

Consider, finally, the following claim about the effects of intervention.

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These are the men who invest in “capital” (land and/or capital goods) used in the productive process. Their function is as we have described: the advance of money to owners of factors and the consequent use of the goods until the more nearly present product is later sold (*ibid.*: 509).

There are many citations to this role in his treatise. Thus, he appears for this to refer to something similar to Mises’s “entrepreneurs and capitalists.” At the same time, it is evident that he aims to reject Mises’s concept of consumer sovereignty. Thus, for Rothbard, the entrepreneur-capitalist role cannot be a mandatory of the consumer. It is as if Rothbard is invoking the Austrian theory of value and cost without, at the same time, accepting the PHRUI. To do this, however, he would have to invoke some other criterion to define utility. Since he rejects utilitarianism, his use of this concept is confusing. In any case, the important point in what follows is that he does not discuss errors made by savers who do not fit into the role of the capitalist-entrepreneur because they are not part of his competitive process.

<sup>10</sup>As an aside, this approach to the subject would render Rothbard’s economics inapplicable to a society in which interventionist decisions are made by a dictator, since voter errors would be irrelevant.

[T]he free market always benefits every participant, and it maximizes social utility ex ante; it also tends to do so ex post, for it contains an efficient mechanism for speedily converting anticipations into realizations. With intervention, one group gains directly at the expense of another, and therefore social utility is not maximized or even increased; there is no mechanism for speedy translation of anticipation into fruition, but indeed the opposite...(ibid.: 891).

Here he writes that only the free market, by which he means his unhampered market economy, tends to benefit every participant. His main concern is intervention. With respect to that issue, he claims to be able to draw the conclusion that social utility is not maximized or even increased as a consequence of intervention. Considering the prospect for error, this claim cannot be correct. Even if we disregard the fact that he had not defined social utility, it is evident from the discussion preceding this statement that the conclusion must assume that the person who carries out the intervention does not intervene in a way that reduces the amount of harm to a person of making decision-making errors. With regard to my discussion of errors by savers and consumers, he admits no policy that would reduce a saver or a consumer's errors. Yet it is easy to conceive of laws that would reduce the propensity for error. These include setting standards for weights and measures, requiring labels on food products, setting accounting standards and legal standards for contracts. I do not mean to claim that these interventions would benefit consumers or savers to a greater extent than the harm they do, no matter how one defines benefit and harm. I only mean to emphasize that to prove his proposition, Rothbard would have had to take account of this possibility. He also does not consider items that modern economists call public goods. It is incumbent upon him to use his imagination to consider the possibility that their supply, through intervention, would contradict his ex post utility proposition about intervention.<sup>11</sup>

It is important to note that Rothbard does not examine each intervention separately and then draw his conclusion about intervention. He does the opposite. He first draws his conclusion, mainly on the basis of

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<sup>11</sup>Of course, Mises also did not consider saver and consumer errors, at least not directly. Nor did he consider public goods. However, his statements about intervention in a real economy were not so sweeping. In general, Mises recommended a cost-benefit analysis, keeping in mind the goal of preserving and expanding the division in accord with the PHRUI.

his definitions of individual sovereignty and the unhampered market economy. Then he turns to evaluating particular policies, using either a nebulous utility standard or his unhampered market economy as an ideal.

### **Critique of Consumer Sovereignty and Mises**

Rothbard criticized consumer sovereignty. His target was not Mises; it was Hutt. His argument is basically against the claim that consumer sovereignty can be used as a criterion to judge whether the action of an individual in a real market economy is good or bad. He says that proper analysis of the free market economy (or free society) shows that to legitimately make this claim, a person must inject his own value judgment concerning what is good. He takes two complementary approaches. The first is to deduce that no price in the unhampered market economy can be unjust. The second is that individuals have a natural right to dispose of any property that they rightfully own. I discuss each in turn.

#### *No Prices in the “Unhampered Market Economy” Can Be Unjust*

His first approach is to use the implications of his definition of the “unhampered market economy.” This approach seems best demonstrated by the following assertion:

If the free-market route – the route of mutual benefit – is adopted, then there can be no other criterion of justice than the free-market price, and this includes alleged “competitive” and “monopoly” prices, as well as the actions of cartels. In the free market, consumers and producers adjust their actions in voluntary cooperation (Rothbard 2004: 636).

When Rothbard writes that the free-market price is his criterion of justice, he is referring ultimately to “individual sovereignty.” “In a purely free society, each individual is sovereign over his own person and property, and it is therefore this self-sovereignty which obtains on the free market. No one is ‘sovereign’ over anyone else's actions or exchanges” (ibid.: 630). Since a free society price is set by means of exchange, it follows that no “unhampered market economy” price or action can be unjust. This applies to the monopoly price.

*A Person Has a Natural Right to Waste Her Property*

The second approach is to apply the assumption of individual sovereignty to personal property to the problem. In the market society or “unhampered market economy,” the rightful owner of property is permitted to dispose of it in any way he wants. It follows that in Rothbard’s market society, one cannot legitimately judge a person’s waste of her own property to be against the interests of others. In that society, the rightful owner’s sovereignty trumps the interests of others. Correspondingly, when Hutt maintains that monopoly may be wasteful, he must be injecting his own values into his analysis. Thus Rothbard writes:

[C]ontrary to Hutt, each individual has self-sovereignty over his person and property on the free market. The producer, and the producer alone, decides whether or not he will keep his property (including his own person) idle or sell it on the market for money, the results of his production then going to the consumers in exchange for their money (*ibid.*: 632).

[S]uppose producer A withholds his labor or land or capital service from the market. For whatever reason, he is exercising his sovereignty over his person and property (*ibid.*: 631).

Rothbard does not consider the most convincing case, which is one where the owner of property intentionally destroys it or allows it to sit idle or go to waste (if it is perishable) because, to sell it she would have to reduce the price at which she sells other property. Instead, he considers the case of a coffee cartel, the members of which shift resources to other endeavors that yield less consumer benefits in a utilitarian sense. He writes:

Suppose...that before the coffee cartel went into operation, X amount of labor and Y amount of land co-operated to produce 100 million pounds of coffee a year. The coffee cartel determined, however, that the most remunerative production was 60 million pounds and therefore reduced annual output to this level. It would have been absurd, of course, to continue wasteful production of 100 million pounds and then to burn 40 millions. But what of the now surplus labor and land? These shift to the production, say, of 10 million pounds of rubber, 50,000 hours of service as jungle guides, etc. Who is to say that the second structure of production, the second allocation of factors, is less “just” than the first? In fact, we may say it is more just, since the new allocation of factors will be more profitable, and hence more value-productive, to consumers (*ibid.*: 638).<sup>12</sup>

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<sup>12</sup>In this example, the cartel does not actually destroy coffee. Thus individuals in the role of the consumers would still get some benefit.

That Rothbard does not consider the most convincing case is more an omission than an error, since the principle he aims to espouse applies to this telling case as well.<sup>13</sup> The principle is that the rightful owners of a resource have an individual sovereignty right to dispose of it as they wish.

### *Rejection of the Distinction Between Consumer and Producer*

Rothbard's conception of the "unhampered market economy" leads him to reject Hutt's distinction between the individual as consumer and individual as producer as a means of helping one to understand market interaction (*ibid.*: 631-2). I have pointed out that Mises expanded on Hutt by defining a praxeologically-based entrepreneur function which is *always* the mandatory of consumers. Against this distinction, Rothbard argues that the categories "producer" and "consumer" are insufficient to be useful in judging whether the a real businessperson is or is not harming others through his monopolistic actions. Rothbard views a monopolist not only as a producer and supplier but also as an individual who has the (ethical) right to do what she wants with her property, regardless of the role assigned by the economist. By rejecting Hutt's distinction between consumer and producer, Rothbard implicitly rejects the notion that the entrepreneur function serves consumers' interest. He thus rejects Mises's consumer sovereignty and, with it, Mises's basis for evaluating interventionist arguments.

### *Mises's Presumed Ethics Are Questionable*

A counterpart of this rejection is Rothbard's claim that Mises's values tainted his analysis of the monopoly price. Rothbard believed that Mises's treatment of monopoly was based on his ethical predispositions. In a 1954 letter he wrote:

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<sup>13</sup>The fact that the resources are shifted to other uses instead of being used to produce coffee is not relevant to Hutt's claim that there is a waste. The reason is that waste, to Hutt, is defined not by whether a resource is used but whether its use is allocatively efficient. Rothbard, who does not accept this definition of waste, probably did not see the destruction of property as his most convincing case. One can only identify the most convincing case if she adopts Hutt's point of view on the matter.

Mises states definitely that whenever a monopoly price is instituted, the concept of “consumer sovereignty” receives a great setback. Mises’s ethics do not permit an outright value-judgment, but the inference is pretty clear that a monopoly price situation is a highly unfortunate one (*ibid*: xliii).

Here he objects to what he interprets as Mises’s excess concern with the propensity of a real-world monopolist to withhold some of his output from consumers. The producer-monopolist has a right, asserts Rothbard, to do with the property as she pleases.

In the excerpt of the letter that I quoted, Rothbard does not say what he means by Mises’s ethics. Moreover, in *Man, Economy and State*, his attack on consumer sovereignty is not aimed at Mises but at Hutt. One must presume, however, that he had in mind the notion that Mises is a utilitarian, which he expressed in a later paper (Rothbard 1976: 104). We have seen earlier in this essay that Mises built his economics around the purpose of being prepared to evaluate interventionist arguments made on the basis the PHRUI. This principle was related to the utilitarianism of the classical economists. However, it was substantively different. In any case, Mises also pointed out that so long as economics addresses itself to the criteria used by those who make interventionist arguments, it can remain value free (Gunning 2005a and 2005b). Rothbard apparently did not recognize that Mises could achieve value freedom by addressing his arguments solely to those who accept the PHRUI,<sup>14</sup>

#### *An Enhancement?*

Rothbard writes that a goal of his *Man, Economy and State* is to fill gaps (Rothbard 2004: xciii). Gaps must be filled for students because, although Mises’s *Human Action* must now be the starting point for constructive work in economics, that treatise “assumes considerable previous economic knowledge and includes within its spacious confines numerous philosophic and historical insights” (*ibid*.). Although

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<sup>14</sup>Rothbard, of course, either did not understand or he disapproved of the PHRUI. This explains why he claimed that Mises’s analysis is tainted by ethics.

Rothbard does not identify the gaps he has in mind, his preview of his book seems to note two of these. The first concerns the price of a durable factor of production. He notes his “resurrection of Professor Frank A. Fetter’s brilliant and completely neglected theory of rent...” (*ibid.*: xciv-xcv). In an effort to fill this gap, Rothbard claims to integrate this theory with “the Fetter-Mises pure time-preference theory of interest” and to add to the theory by separating factors into those that are original and those that are produced. The second gap, I surmise, is in monopoly theory. Rothbard proposes to present “a completely new theory of monopoly – that monopoly can be meaningfully defined only as a grant of privilege by the State, and that a monopoly price can be attained only from such a grant” (*ibid.*: xcv).

I have shown that Rothbard’s effort to make the second “enhancement” resulted in his rejection of Mises’s goal of putting the economist in a position to make value-free evaluations of interventionist arguments. Since all of the economic theorems developed by Mises require an acceptance of principle of consumer sovereignty, his rejection of this principle amounts to an implicit rejection of Mises’s economics. It follows that one must reject the Rothbard’s claim that he enhanced the Austrian theory of monopoly.

### *Purpose*

Aside from making these “enhancements,” Rothbard’s stated purpose is, like Mises’s, to employ his economic theory to evaluate interventionist arguments. Thus, his concluding chapter presents a typology of intervention, discusses its direct and indirect consequences and the effects on utility, and sets forth a necessarily brief analysis of the various major types of intervention, including price control, monopoly grants, taxation, inflation, and government enterprise and expenditures (*ibid.*). Also like Mises, in his conclusion, he writes about an ultimate goal. I discuss this ultimate goal in the next part, where I compare Rothbard with Mises.

### 3. COMPARISON OF MISES AND ROTHBARD

To further elucidate the difference between Mises and Rothbard, this section compares the two authors on an issue that both regarded as crucial: the purpose of economics in relation to praxeology. Following this, I compare the two on a specific policy issue that neither considered – that of a specific proposal to deal with pollution. My aim is to illustrate their differences with a concrete example.

#### **Purpose of Economics in Relation to Praxeology**

To the non-discriminating reader, Rothbard's closing statements in his *Man, Economy and State* are similar to those of Mises's closing statements in *Human Action*. The truth is that they are quite different. Rothbard's conclusion consists of three tightly reasoned, and largely mutually exclusive paragraphs. Each manifests a difference. In this subsection, I discuss each in turn.

#### *Different Criteria for Defining Benefits: the Case of Monopoly*

To avoid misinterpretation, I try to carefully analyze Rothbard's wording. I begin by quoting the first paragraph.

We have thus concluded our analysis of voluntary and free action and its consequences in the free market, and of violent and coercive action and its consequences in economic intervention. Superficially, it looks to many people as if the free market is a chaotic and anarchic place, while government intervention imposes order and community values upon this anarchy. Actually, praxeology – economics – shows us that the truth is quite the reverse. We may divide our analysis into the direct, or palpable, effects, and the indirect, hidden effects of the two principles. Directly, voluntary action – free exchange – leads to the mutual benefit of both parties to the exchange. Indirectly, as our investigations have shown, the network of these free exchanges in society – known as the “free market” – creates a delicate and even awe-inspiring mechanism of harmony, adjustment, and precision in allocating productive resources, deciding upon prices, and gently but swiftly guiding the economic system toward the greatest possible satisfaction of the desires of all the consumers. In short, not only does the free market directly benefit all parties and leave them free and uncoerced; it also creates a mighty and efficient instrument of social order. Proudhon, indeed, wrote better than he knew when he called “Liberty, the Mother, not the Daughter, of Order” (*ibid.*: 1024).

I have shown that Rothbard's free market refers to a situation in which all property is owned by the rightful owners, as determined in accord with the principle of individual sovereignty. In this paragraph he describes two principles that economics teaches about such a situation. The first one is self evident – that voluntary action leads to individual benefits. This is true regardless of the presence of free market conditions. The second and most telling principle is the second one – that voluntary action in the free market leads to the indirect result of “the greatest possible satisfaction of the desires of all the consumers.”

This principle differs from that of Mises in two ways. First, while Mises emphasizes that monopoly is an exception, Rothbard does not admit this exception. On the basis of my presentation of the two views in parts 1 and 2 of this essay, the reader now knows that the difference is due to the different images of the market economy used by the two authors. Mises draws his conclusions on the basis of his image of the pure market economy, in which rights to control actions that cause external effects are owned exclusively by single individuals. In this economy, individuals are fully responsible for PHRUI-evaluated damage they cause others and are rewarded fully for the PHRUI-evaluated benefits they confer. Damage and benefits are defined in terms of the effect on the division of labor. Rothbard draws his conclusion on the basis of his image of the unhampered market economy. Private property rights are established in accord with the ethical principle of individual sovereignty. The owner of property can use or not use it in any way she wants. As a result, she cannot fully be the mandatory of the consumer. Even if she charges a monopoly price, her action results in the greatest possible satisfaction since the benefits to the rightful owner, which she must necessarily be, trump the benefits to others, however measured. Rothbard's purpose is to draw out the implications of a society in which all actions are now, and always have been, based on the ethical criterion of individual sovereignty. One must presume that his ultimate purpose is to promote the use of this criterion.

Mises's purpose is to evaluate interventionist arguments pertaining to real economies in which there are private property rights, free enterprise and the use of money. He builds an image of the pure market economy

as a means toward that end. In a real economy, both monopoly and external effects may be present. Each interventionist argument must be evaluated without bias, considering all of the PHRUI-evaluated benefits and harm in the presence of and absence of the intervention.

### *Different Treatment of Coercion*

The second paragraph of Rothbard's conclusion is about coercion:

On the other hand, coercion has diametrically opposite features. Directly, coercion benefits one party only at the expense of others. Coerced exchange is a system of exploitation of man by man, in contrast to the free market, which is a system of cooperative exchanges in the exploitation of nature alone. And not only does coerced exchange mean that some live at the expense of others, but, indirectly, as we have just observed, coercion leads only to further problems: it is inefficient and chaotic, it cripples production, and it leads to cumulative and unforeseen difficulties. Seemingly orderly, coercion is not only exploitative; it is also profoundly disorderly (*ibid.*: 1025).

For Rothbard, the use of coercion cannot yield results that benefit individuals. How different this is from Mises. Mises regarded the use of coercion as a requirement for the enforcement and also largely for the establishment of private property rights and control of fraud. Whereas Rothbard's view suggests that a viable market economy is possible without coercion, Mises's view denies the possibility of a viable market economy without coercion.

### *Different Approaches to Value Freedom in Economics*

Rothbard's concluding paragraph can be used to help identify key differences between Rothbard and Mises on their conceptions of praxeology and economics:

The major function of praxeology – of economics – is to bring to the world the knowledge of these indirect, these hidden, consequences of the different forms of human action. The hidden order, harmony, and efficiency of the voluntary free market, the hidden disorder, conflict, and gross inefficiency of coercion and intervention – these are the great truths that economic science, through deductive analysis from self-evident axioms, reveals to us. Praxeology cannot, by itself, pass ethical judgment or make policy decisions. Praxeology, through its *Wertfrei* laws, informs us that the workings of the voluntary principle and of the free market lead inexorably to freedom, prosperity, harmony, efficiency, and order; while coercion and government intervention lead inexorably to hegemony, conflict, exploitation of man by man, inefficiency, poverty, and chaos. At this point, praxeology retires from the scene; and it is up to the citizen – the ethicist – to choose his political course according to the values that he holds dear (*ibid.*: 1025).

Mises would not object to the first sentence. However, one word in the second sentence would surely draw his criticism. This is the word “coercion.” The difference in treatment of coercion by the two authors was described in the previous subsection of this part of the essay. Also in the second sentence, Rothbard says that economic science consists of “deductive analysis from self-evident axioms.” This is not exactly so. Praxeology consists of such analysis. Economics, however, deals with the real world. To produce economic theorems, one must combine the deductions of praxeology with assumptions that are relevant to the theorems one aims to produce (Mises 1966: 65). And these theorems must be relevant to the evaluation of some interventionist argument (*ibid.*: 238). One who aims to evaluate an interventionist argument made by people who live in the real world must build an image of a market economy that is relevant to the argument. Did Rothbard recognize, as Mises had pointed out, that such auxiliary assumptions are necessary in order to do economics, as opposed to praxeology? On the one hand, he recognized that economics is a branch of praxeology (Rothbard 2004: 72-76). He also stated at one point that most of his treatise was based on a combination of the deductions of praxeology and subsidiary assumptions (*ibid.*: xciv, 2n). However, in his general statements about praxeology and economics, he ordinarily disregarded the auxiliary assumptions, as he did in this conclusion. Accordingly, Rothbard’s quoted statement about economics being a deductive science is incomplete and probably misleading.

More important is his reference to *Wertfrei* laws. To Mises, value freedom is achievable because of the assumption that both a proponent and opponent of intervention accept the PHRUI. Acceptance of this principle is based, in turn, on acceptance of the principle of the higher productivity of the division of labor. Economics can avoid judgments of value because economists investigate “whether a measure...can bring about the result...for the attainment of which it is recommended” (Mises 1966: 883).

Rothbard does not discuss the source of value freedom. He seems to accept the view that because economic theorems are derived logically from fundamental axioms and real world postulates, they must be

value free. This view is not incorrect. However, theorems derived in this way can also be irrelevant to any specific purpose. The only way to make them relevant is to define the more fundamental task, or goal. Mises's fundamental goal was to provide a means for evaluating interventionist arguments made on the basis of the PHRUI. Rothbard's goal is similar in that he wants to provide a means for evaluating proposals to intervene. However, since he disregards criteria that others typically use to evaluate such arguments, he has no way to make his economics relevant except to shift the goal away from the evaluation of interventionist arguments to the evaluation of the criteria themselves. So he presents his own criterion – that of individual sovereignty, which he regards as superior. Thus, he concludes that “it is up to the citizen – the ethicist – to choose his political course according to the values that he holds dear” (ibid.: 1025, as quoted above). Whatever one may think of this procedure, Rothbard's conception of the aim of economics is quite different from that of Mises. Mises did not leave the decision of whether an intervention should be made up to the citizen. He assumed that the maker of an interventionist argument accepts the PHRUI. One who refuses to use this criterion, he would maintain, must either be an ascetic or a person who denies the greater productivity achievable through a division of labor.

### **Evaluation of a Pollution Policy**

Consider a proposal to use the coercive power of government to establish a system of air pollution emission permits. In other words, the proposal's aim is to establish private property rights to pollute the air. The avowed purpose of the proposal is to reduce the hazard to health that I assume is scientifically established as being due to air pollution by local factories. Government agents determine the amount of acceptable pollution and then auction off legal rights to emit that quantity. Coercion by government agents is needed in order to deter those who are not assigned such rights from performing polluting acts.

For Mises, the policy argument favoring intervention could be evaluated by building an image of two economies. The first is a market economy that is pure in all respects except for the absence of relevant private property rights in unpolluted air and the consequent presence of relevant external effects. The second is a market economy that is similar to the first in all respects except that it contains the coercion proposed in an interventionist argument to be used against those who cause the external effects. The builder of the images would assume that the maker of the interventionist argument used the criterion of the PHRUI to make judgments. Accordingly, he would build images that compare the extent to which consumer sovereignty prevails in the two cases. Such images would attempt to provide a comparison of performance of the entrepreneur function under the two sets of conditions.<sup>15</sup>

A practical question would seem to immediately arise about whether such an approach might lead to the violation of previously established private property rights. Suppose, for example, that a former group of citizens had previously agreed to permit factories to pollute. A town meeting had been held at which citizens had decided that, in spite of the prospect for damage due to pollution, they would permit factories to pollute to a reasonable level. The new law proposes to cut back the pollution from the previous amount without gaining the agreement of the polluters.

Since Mises did not give an example of a law that aimed to deal with external effects, his writings provide no guidance concerning how to deal with this practical issue. Strictly speaking, Mises's analysis can only be strictly applied to a case in which no private property rights are known to exist. I have referred to this as a case of contestable private property rights. In the case of contestable private property rights, I would presume that absent a strong claim to a legal right to perform or block the action that causes the external

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<sup>15</sup>The economist's task would be complete after the images were built. However, there would remain the task of identifying the costs of employing coercion in this specific way. I am referring here to the costs of making and enforcing the law that is necessary to implement the intervention.

effect, Mises would suggest a comparative analysis, as I described. I reach this conclusion on the basis of his statement that every interventionist argument must be fully scrutinized.

For Rothbard, the evaluation would take a different path, although it is not certain which path. One possibility would be to assume that the pollution is an invasion of the individual sovereignty of a single person who first used the unpolluted air that is in question. If that person had sold rights to the air or given it away to new residents, then they would also be part rightful owners. In this event, the unpolluted air would be collectively owned. In either case, the pollution permit policy could be approved only if the original owner or the unanimous collective of current co-owners of unpolluted air agreed to allow the policy. If no rights had been sold or given away, the government should use its violence to compel the invader to stop her activity.

We can immediately see the difficulty with this approach. It is unlikely that the first user of the unpolluted air would have regarded it as a resource. Many users, including those who are now the cause of the external effects are most likely to have already been using the unpolluted air before anyone came to regard it as a resource. Moreover, the first user, along with other initial users, may have moved or died. The basic problem is that, at the time that the external effect becomes relevant – i.e., at the time that residents begin to recognize that they are harmed by pollution – ownership of the unpolluted air is *contestable*. Because of this, there is no obvious way, according the principle of individual sovereignty, to determine who owns the air. Yet Rothbard's unhampered market economy has no procedure, or hint of a procedure, for dealing with contestable property rights.<sup>16</sup>

Two facts about existing property rights are (1) that most property is not possessed by the rightful owners and (2) that the rightful owners are either dead, not capable of being identified, or capable of being identified

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<sup>16</sup>One might wish to claim that Rothbard left this kind of work up to others who would apply his general framework. One such effort was made by Cordato (1992), as mentioned above. Cordato's effort, however, also contains no procedure for dealing with property rights that are genuinely contestable. See the initial critique in Gunning (2000a), Cordato's response (Cordato 2000), and my reply (Gunning 200b).

but only at a prohibitive cost. To decide how to apply government coercion to enforce the legal rights associated with Rothbard's unhampered market economy, judges would have the task of investigating the complete history of the property rights in question. Absent such an investigation and judgment, there would be no way to apply Rothbard's principle of individual sovereignty.

Whereas Mises's approach is reasonably consistent with the neoclassical economics of the majority of economists, Rothbard's seems impossible to apply. Some Rothbard followers ignore the fact that few existing private property rights are possessed by their rightful owners. They also ignore or gloss over the contestableness of many existing rights. Having done this, they are in a position to criticize practically every government use of coercion on the grounds that, under the assumptions they make (and the ethic they apply), no government use of coercion is justified. One can only say about such followers that they are not doing economics either in the traditional sense or in the Austrian sense.

#### 4. CONCLUSION

Both Mises and Rothbard built images of market economies and then sought to evaluate government restrictions. In this sense, their two works were similar. Beyond this, however, their purposes were quite different and their evaluations incomparable. Mises built his image of the pure market economy in a way that was specifically designed to evaluate interventionist arguments that are made by individuals who accept the PHRUI. He defined the entrepreneur function to represent all action in a pure market economy that results in the satisfaction of the wants of individuals in the consumer role. The entrepreneur function obeys the principle of consumer sovereignty. The entrepreneur is the mandatory of the consumer. The pure market

economy image was designed to help evaluate all sorts of PHRUI-based interventionist arguments, including those associated with external effects due to incomplete private property rights.

Mises did not invent consumer sovereignty. Nor did he invent the entrepreneur function. This was done by the non-mathematical neoclassical economists who preceded him. However, he provided the praxeological basis for it with his analogy between the isolated actor satisfying his own wants and the entrepreneur satisfying the wants of individuals in the consumer role. In essence, Mises followed the tradition of the classical economists. But he did more than this. His praxeological foundation gave economists a means of protecting themselves against the attacks by writers who subscribed to the ideas of “irrationalism, historicism, panphysicalism, behaviorism, and all varieties of polylogism” (Mises 1966: 7).

Rothbard built his image of the unhampered market economy on the basis of the assumption that individual sovereignty prevails – that there are no invasions of person or of rightfully acquired property. By defining the “unhampered market economy” in this way, he molded his own creation – an economics that rejects the traditional criterion for evaluating interventionist arguments in favor of an individual sovereignty criterion. Similarly, he rejected the traditional definition of private property. In doing this, he gave up any hope of being part of the economics tradition founded, or enhanced, by Mises. He rejected consumer sovereignty for the same reason that he rejected the tradition of economics. It did not accord with his individual sovereignty ethic.

Rothbard asserted that Mises’s support for consumer sovereignty was based on his ethics. He did not realize that what he called Mises’s ethics was a manifestation of the link Mises provided between his economics and the classical economics tradition. Rothbard broke the link between his economics and that of both Mises and the tradition. Whether he realized this or not, he apparently aimed to produce an Austrian economics based on the ethic of individual sovereignty and the assumption that the rightful owners of property could be determined.

In rejecting Mises's and traditional economics, Rothbard closed the door to the evaluation of arguments about a market economy on any other grounds than his ethic of individual sovereignty. As a result, it is impossible for those who follow Rothbard to deal with an argument that maintains that intervention is necessary because individuals in the consumer role would be better off as a result. At the same time, Rothbard opened the door for his followers to claim that there is economic justification for asserting that all government intervention is invasive and, therefore, bad. It is not surprising that some of these followers have become anarchists.

Rothbard said that at least one goal of his *Man, Economy and State* was "to isolate the economic, fill in the interstices, and spell out the detailed implications, as I see them, of the Misesian structure" (Rothbard 2004: xciv, as quoted above). Another was to present his theory of monopoly. "In this theory, there can be no monopoly or monopoly price on the free market" (*ibid.*: xcv). Unfortunately for those who hope to find some hint of Misesian economics in the writings of Rothbard, this rejection marked an inexorable split with Mises. In rejecting consumer sovereignty, Rothbard had to also reject the special definitions and elucidations of entrepreneurship that Mises meticulously developed. Along with this, he had to reject Mises's description of the market process. Rather than fill in interstices, Rothbard sought to cover it with a tarp.

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