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**The Austrian School in the American Economic Review
(1911-2004): The Initial and Final Decades**

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Abstract: Reference to an Austrian or neo-Austrian economist has appeared in the American Economic Review each year since the journal was first published in 1911. Topics examined in the first (1911-20) and last decades (1995-2004) of the AER's publication include mathematics' role in economics, the business cycle, and government central planning and interventionism.

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1 Introduction

The American Economic Review (AER), first published in 1911, is one of the leading economic journals in the United States. An important measure of the AER's preeminence: 13 Presidents of the American Economic Association, which publishes the quarterly journal, have won the Nobel Prize in Economics.¹ An AER Editor who never served as President also won the prize.²

Bank of England Governor Mervyn King's (AER2004, 1-13, a) reference to Austrian economists Carl Menger (1892) and Friedrich A. Hayek (1976) marked the 94th consecutive year that Austrians have been cited in the AER.³ This impressive history of publication includes references to traditional Austrians like Menger, Hayek, Eugen von Bohm-Bawerk, Ludwig von Mises, Richard von Strigl, Friedrich von Wieser, Murray N. Rothbard, Israel Kirzner, and Hans Sennholz. It also includes neo-Austrians such as Joseph Schumpeter, Gottfried Haberler, Fritz Machlup, Benjamin M. Anderson, and Oskar Morgenstern. Far from being non-credible, the Austrian School remains relevant in the pages of one of America's leading economic journals.

A reference to an Austrian or neo-Austrian economist has appeared in the AER each year since the journal was first published in 1911 (Appendix). This review is a brief survey of references to the Austrian School in the initial (1911-1920) and final decades (1995-2004) of the AER's history. Topics covered in references to the Austrian School in both periods include the role of mathematics in economics, the business cycle, and central planning and Hayek's problem of knowledge. Some references in the AER's initial decade anticipated the final decade. Schumpeter's observation about mathematics' limitations was discounted as econometrics emerged to dominate the AER. His insights about the

¹ Eleven economists served as AEA President prior to being awarded the Nobel: Paul A. Samuelson (*AEA* 1961, Nobel 1970), Simon Kuznets (1954, 1971), Wassily Leontief (1970, 1973), Milton Friedman (1967, 1976), Lawrence R. Klein (1977, 1980), James Tobin (1971, 1981), George J. Stigler (1964, 1982), Franco Modigliani (1976, 1985), Robert M. Solow (1979, 1987), Gary S. Becker (1987, 1992), Amartya Sen (1994, 1998). Two economists served as AEA President after being awarded the Nobel: Kenneth Arrow (*AEA* 1973, Nobel 1972), Robert E. Lucas, Jr. (2002, 1995).

² Joseph S. Stiglitz was AER Editor (1986-1993) and was awarded the Nobel in 2001.

³ Garicano and Santos (*AER*2004, 499-525), one month after Governor King's remarks, started their essay by citing Hayek (*AER*1945, 519-30) on the knowledge problem: "The peculiar character of the problem of a rational economic order is determined precisely by the fact that the knowledge of the circumstances of which we must make use never exists in a concentrated or integrated form."

business cycle fared better. Anderson reviewed central planning in World War I, and Hayek's "knowledge problem" was cited in the final decade. Some issues, it appears, are eternal in economics. Von Mises' and Anderson's early criticism of the quantity theory, however, was not echoed in the AER's final decade.

2 The Initial Decade (1911-1920)

The Role of Mathematics

Austrian skepticism about the role of mathematics in economics appeared in the AER's first year of publication. Wicker (AER1911, 318-20) is the first reference in the AER to an Austrian or neo-Austrian. Schumpeter's *Das Wesen* (1908) is termed "revolutionary", and deemed "deserving of more attention and consideration than it has received from American and English economists." Wicker praises Schumpeter's scholarship, observing:

One of the most valuable features of the book lies in its discussion of the views of other economists. This discussion, which constitutes in the aggregate a large part of the volume, is quite unusually catholic and kindly. It reveals a closely critical knowledge of the economic literature of the nineteenth century, both European and American.

Wicker notes a theme of the book is, "Economic dynamics can never be an 'exact' science." Mathematics should be limited to "the field of statics".

The Business Cycle

A reference to the business cycle appeared in the AER's second year. Clark (AER1912, 873-75) cites Bohm-Bawerk's "brilliant studies" of "time an element in production" and "capitol and organization" in his review of Schumpeter (1912). He notes Schumpeter's analysis of the business cycle: examines "commercial crises and treats them very properly as dynamic phenomena—the outcome of a certain unbalanced and uneven progress." Clark observes that Schumpeter "draws a distinction between the kind of change which presents no serious problems for solution and the kind which creates such problems."

Population growth and “enlargement of the fund of capital would call for adaptations which would take place automatically and steadily,” he notes, “while the coordinations made by entrepreneurs cannot act evenly and extend throughout the whole system at once.”

Monetary Policy: Criticism of the Quantity Theory

Austrian criticism of the quantity theory of money appeared in the AER’s third year. Lutz (AER1913, 144-46) is a critical review of Von Mises (1912). Austrian criticism of the quantity theory of money and the use of index numbers is reviewed. Von Mises contends that while the quantity theory “contains a germ of truth in the proposition that the demand for and the supply of money are conditions which affect its value, it does not afford an adequate explanation of the value of money.” Index numbers “may be of some use in ascertaining objective use-value”, this “is of relatively little significance, compared with the subjective significance of a given money quantity.” Index numbers may render a useful service, but they are “of no significance for the development of the theory of the value of money.” Lutz is critical. “The work under review,” he writes, “apparently represents an effort to develop a theory of money which will be in accord with the utility theory of value in its most extreme subjective applications.” He concludes “the thoroughgoing application of this theory in all of its detail leads to mainly negative results.” Lutz rejects this explanation, arguing “there are certain external objective phenomena of price which may be known, recorded, and studied; and on the basis of these objective manifestations safe conclusions may be drawn regarding the course of prices and its relation to human welfare.”

Anderson (AER1916, 168-69, s) continues this Austrian criticism of the quantity theory:

It is, moreover, quite grotesque for static theory to offer itself as a support for its own foundations. A static or “normal” theory of money and credit, resting on the notion of accomplished equilibrium, after transitional changes have been effected, misses the main point as to the function of money and credit. Static theory which assumes frictionless fluidity, misses the whole point concerning money and credit. A functional theory of money and credit must be a dynamic theory, basing itself on

an analysis of friction, of transitions, and the like. And this is one reason, among many, why I find the quantity theory of money indefensible.

Wicksell (AER1919, 927) is an abstract reference to an article critical of Anderson's attack on the quantity theory. Phillips (AER1920, 137-40) also notes Anderson's quantity theory criticism.

Other Monetary Policy

Johnson (AER1914, 113-16) is a review of Bohm-Bawerk (1912). Johnson explains a "large proportion of the literature on interest during the last two decades has centered on Bohm-Bawerk's theory:" He continues, "It may fairly be said that a primary classification of economic theorists is based upon the acceptance or rejection of Bohm-Bawerk's interest doctrine." Bohm-Bawerk's "frequent contributions to the periodical literature of economics has offered sufficient evidence that he has allowed little of the vast volume of criticism to escape him," Johnson notes, reviewing the Austrian's response to Alfred Marshall and Irving Fisher. Johnson finds Bohm-Bawerk's system "logically unassailable" except for "the single exception of the treatment of the relation of productivity to the interest rate."

The passing of Bohm-Bawerk (1851-1914) is noted (AER1915, 947-48) in an abstract reference to Schumpeter's memorial (1914). Schumpeter's tribute is termed, "A keenly sympathetic summary and appreciation by a pupil and colleague."

Mitchell (AER1916, 140-61, s) cites Bohm-Bawerk (145n), Menger (143-44), von Wieser (148n) and Schumpeter (150) in his paper on monetary policy. He writes, "Among recent tendencies in economic theory none seems to me more promising than the tendency to make the use of money the central feature of economic analysis."

Anderson is cited on the limits of fiscal policy in Davenport (AER1917, 1-30).

Central Planning

Anderson (AER1918, 239-56) is a review of U.S. government price-fixing during World War I. "The more prices the government undertakes to control," Anderson concludes,

“the greater the difficulties involved.”

Anderson (AER1919a, 192) opposes peacetime central planning, arguing, “Artificial control of business and prices should be dispensed with as early as possible.” Opposition continues in Phillips (AER1920, 137-40), a review of Anderson (1919b), termed “interpretive and critical, (a) finely and judicially critical, record” for both countries of “economic transformations” as a result of WWI. This includes Anderson’s scathing and convincing condemnation of the policy of restricting gold payments within the U.S. and abroad.

3 The Final Decade (1995-2004)

The Role of Mathematics

The AER was dominated in the final decade by econometrics. The majority of references to the Austrian School are in articles that use econometrics to examine issues. The methodology is questionable, but the breadth of topics examined by models is remarkable, including pari-mutuel betting, migration, trade, reputation, and truckers. It appears there is no problem that econometrics cannot solve.

Hurley and McDonough (AER1995, 949-56) consider the Hayek hypothesis as it relates to the favorite-longshot bias in parimutuel betting (favorites win more often than the betting odds indicate, and longshots win less often than the betting odds indicate). The Hayek hypothesis, according to Nobel laureate Vernon L. Smith (1982), suggests that markets can work efficiently even when participants have a limited knowledge of the environment or of other participants.

Hurley and McDonough conclude:

Our model suggests that the subjective win probability on a favorite, or near favorite, ought to be bounded above by its objective probability adjusted for track take. This hypothesis appears to be supported by the empirical findings of other researchers. However, the empirical results of two parimutuel-betting experiments are not consistent with this argument. The firm conclusion of this paper is that the bias on the favorite is not explained by costly information and transaction costs.

Carrington, Detragiacha and Vishwanath (AER1996, 909-30) cite Higgs in a footnote

(1976) in presenting a “dynamic model of migration in which moving costs are declining with the stock of migrants” in the U.S. The authors conclude, “The boll weevil and WWI provided the impetus for a migration process that continued even as the North-South wage gap shrank.” This interpretation, they write, is consistent with the views of others, including Higgs who “emphasize the endogenous dynamics of migration.”

Schumpeter (1942) drives technological change in the model developed by Dinopoulos and Segerstrom (AER1999, 450-72) that “presents a dynamic general equilibrium model of R-&-D-based trade between two structurally identical countries in which both innovation and skill acquisition rates are endogenously determined.” They conclude:

Trade liberalization increases R-&-D investment and the rate of technological change. It also reduces the relative wage of unskilled workers and results in skill upgrading within each industry when R-&-D is the skilled-labor intensive activity relative to manufacturing of final products.

Horner (AER2002, 644-63) cites Hayek (1946) and Schumpeter (1950) in a paper that “shows how competition generates reputation-building behavior in repeated interactions when the product quality observed by consumers is a noisy signal of firms’ effort level.” Horner develops a model, and concludes the “threat of exit induces good firms to choose high effort, allowing good reputations to be valuable, but its uncompromising execution forces good firms out of the market.” Economists’ assumptions that “market participants have complete knowledge of all relevant factors” has “long been criticized as limiting the applicability of the theory, especially when competition is thought of as a dynamic process,” as Austrian economists view the issue.

Collins (AER2001, 272-86) cites Higgs (AER1977, 236-45). His model examines fair employment practices in U.S. labor markets during World War II.

Central Planning

Hayek’s seminal essay (AER1945, 519-30) on the knowledge problem in economics is cited by Williamson (AER2002, 438-43), which examines private ordering in contracts.

Hubbard (AER2003, 1328-1353) cites Hayek (AER1945, 519-30) in developing a model that examines capacity utilization gains from on-board computers in the trucking

industry. Hayek's "famous analysis of economic organization," he writes, "are at the core of a recurring theme in the productivity literature: the premise that information technology (IT) offers opportunities for large productivity gains." To Hayek, "understanding relationships between informational and resource allocation improvements is central for understanding the performance of economic organizations, and how decreases in information costs lead to increases in welfare."

The Business Cycle

Harberger (AER1998, 1-32, a) discusses the cycle as it relates to total factor productivity (TFP). "To me," Harberger states, "Joseph A. Schumpeter's vision (1934) of 'creative destruction' captures much of the story. What he is saying is, yes, it's a jungle out there, but the processes of that jungle are at the core of the dynamics of a market-oriented economy. They are what got us to where we are, and they hold the best promise for further progress in the future." He writes:

Schumpeter saw through to the essence of the problem, but it is not wise for us to be fatalistic in accepting his vision. We cannot lose by making a major effort to understand the process of TFP improvement where it happens—at the level of the firm. This is all the more true because of the performance of negative as well as positive TFP performance.

Other References

Sen (AER1995, 1-24, a) cites Hayek (1960) on the idea of "personal domains" and "protected spheres" in a footnote.

Chow (AER1997, 321-327, s) argues Hayek's conception (1949) of individualism as "an ideal in a Western market economy" is in conflict with China's economic system. Chow contends "individualism versus the collective good" is among "the challenges of the market economy in China" for economic theory. The ideal of individualism, Chow writes, "is not generally accepted in Asian countries. Individual rights may be in conflict with the common good . . . In Asian societies, the common good is often considered to be more important than individual rights. Not only is individual freedom restricted,

but members of a society are educated to serve the society.” According to Chow, market economies have functioned with a limited amount of political freedom in mainland China and other Asian countries.

Schumpeter’s “perennial gale of creative destruction” makes another appearance in Schmalensee (AER2000, 192-96, s), which presents a case for software markets as “Schumpeterian” in an article on U.S. antitrust issues. Schmalensee quotes Schumpeter (1950, 84), “This gale is driven not by price competition, but by competition from the new commodity, the new technology . . . competition which strikes not at the margins of the profits of the existing firms but at their foundations and their very lives.”

Goeree and Holt (AER2001, 1402-22) cite von Neumann-Morgenstern (1944) on game theory.

4 Conclusion

A brief survey of references to the Austrian School in the initial (1911-1920) and final decades (1995-2004) of the AER’s history reveals three topics common to both periods: mathematics’ role in economics, the business cycle, and government central planning and interventionism.

There is clarity of Austrian views in the initial decade. These include skepticism about mathematics role in economics; early Schumpeterian cyclical insights that would flower in the 1930s and 1940s, with variants of Austrian Business Cycle Theory (ABCT) developed by Hayek and von Mises; and a trenchant assault on the quantity theory led by B.M. Anderson, Jr.

The Austrian viewpoints presented in the final decade are inchoate and largely ironic. How ironic that a School known for its skepticism of econometrics should have some of its greatest works by Hayek and Schumpeter co-opted by mathematical economists for their econometric models. If the Austrian School was irrelevant or non-credible it would be ignored in the pages of one of America’s leading economic journals. Yet the frequent references to Austrians, even in these econometric models, only serves to reinforce the School’s importance nearly one century after Menger, Bohm-Bawerk, von Mises, Schumpeter and Anderson first appeared in the AER.

5 Appendix

Austrian and neo-Austrian economists appeared in the *American Economic Review* in the following chronological order:

- (1911) Schumpeter
- (1912) Schumpeter
- (1913) Von Mises
- (1914) Bohm-Bawerk
- (1915) Bohm-Bawerk
- (1916) Austrian School, B.M. Anderson, Bohm-Bawerk, Menger, Schumpeter, Von Wieser
- (1917) B.M. Anderson
- (1918) B.M. Anderson
- (1919) B.M. Anderson
- (1920) B.M. Anderson
- (1921) Austrian School, B.M. Anderson
- (1922) B.M. Anderson, Bohm-Bawerk, Schumpeter
- (1923) B.M. Anderson, Von Mises
- (1924) Schumpeter
- (1925) Bohm-Bawerk
- (1926) Bohm-Bawerk
- (1927) Austrian School, Bohm-Bawerk, Menger, Morgenstern. Schumpeter, Von Strigl, Von Wieser

- (1928) Austrian School, Bohm-Bawerk, Morgenstern, Schumpeter
- (1929) B.M. Anderson, Bohm-Bawerk, Menger, Von Mises
- (1930) Austrian School, Bohm-Bawerk, Haberler, Hayek, Ropke
- (1931) Bohm-Bawerk, Schumpeter
- (1932) Von Mises
- (1933) Haberler, Hayek
- (1934) Hayek, Machlup, Morgenstern; Von Mises
- (1935) Hayek, Machlup, Von Mises
- (1936) Haberler, Ropke
- (1937) Machlup, Morgenstern, Ropke, Von Mises
- (1938) Haberler, Machlup, Ropke , Von Strigl
- (1939) Haberler, Machlup, Menger, Schumpeter, Von Mises
- (1940) B.M. Anderson, Machlup, Morgenstern
- (1941) Hayek, Machlup, Schumpeter
- (1942) Haberler, Machlup, Schumpeter
- (1943) Haberler, Machlup, Von Mises
- (1944) Haberler, Schumpeter; Von Mises
- (1945) Haberler, Hayek
- (1946) Hayek, Machlup, Schumpeter
- (1947) Haberler, Machlup
- (1948) Haberler, Morgenstern
- (1949) Haberler, Machlup, Morgenstern, Schumpeter

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- (1950) Machlup, Schumpeter, Von Mises
(1951) Morgenstern, Rothbard
(1952) Bohm-Bawerk, Machlup, Menger, Schumpeter, Von Wieser
(1953) Haberler, Machlup
(1954) Haberler, Hayek, Schumpeter
(1955) Bohm-Bawerk, Machlup, Morgenstern
(1956) Lachmann
(1957) Machlup
(1958) Sennholz
(1959) Schumpeter, Von Mises
(1960) Machlup
(1961) Hazlitt, Machlup
(1962) Schumpeter
(1963) Machlup, Rothbard, Sennholz, Von Mises
(1964) Haberler, Machlup, Morgenstern
(1965) Machlup
(1966) Haberler
(1967) Machlup
(1968) Kirzner, Machlup
(1969) Hayek, Machlup, Schumpeter, Von Mises
(1970) Machlup, Morgenstern, Schumpeter
(1971) Machlup

- (1972) Haberler, Hayek
- (1973) Bohm-Bawerk
- (1974) Bohm-Bawerk, Hayek, Machlup, von Mises
- (1975) Hayek
- (1976) Machlup, Schumpeter
- (1977) Haberler, Higgs, Machlup
- (1978) Schumpeter
- (1979) Morgenstern
- (1980) Haberler
- (1981) Austrian School, Bohm-Bawerk, Hayek, Menger
- (1982) DiLorenzo, Hayek, Higgs, Schumpeter
- (1983) Hayek, Holcombe, Schumpeter
- (1984) DiLorenzo; Higgs, Schumpeter
- (1985) Austrian School, Bohm-Bawerk, Garrison, Hayek, Rothbard, Von Mises
- (1986) Hayek, Higgs, Menger
- (1987) Machlup, Morgenstern
- (1988) Machlup, Schumpeter
- (1989) Haberler, Hayek
- (1990) Schumpeter
- (1991) Hayek, Morgenstern
- (1992) Hayek, Mintz, Schumpeter
- (1993) Morgenstern, Schumpeter

- (1994) Hayek, Menger, Mintz, Schumpeter
- (1995) Hayek
- (1996) Higgs
- (1997) Hayek
- (1998) Schumpeter
- (1999) Schumpeter
- (2000) Schumpeter
- (2001) Higgs, Morgenstern
- (2002) Hayek, Schumpeter
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(Leading AER articles are marked (a), annual meeting supplements (s), all other articles are reviews)