

FROM MISES TO MORGENSTERN: AUSTRIAN ECONOMICS DURING THE STÄNDESTAAT

HANSJÖRG KLAUSINGER

In the 1930s the Austrian School of economics lived through a crucial phase in its development, which led from the height of its influence at the beginning of the decade to its decline and dissolution after 1945. The rise and fall of the Austrian School and of its liberal¹ wing in particular had its counterpart in the fate it experienced in its country of origin. On the one hand, Austria (and especially Vienna) had played a vital role as a center of communication for all the members of the school. And on the other hand the Austrian Economists in turn had tried to use their reputation for influencing the course of Austrian economic policy, in particular during the Great Depression—and indeed some observers, contemporary and modern, trace the comparatively weak performance of the Austrian economy back to the harmful impact of the Austrian Economists' ideas.

HANSJÖRG KLAUSINGER is a professor of economics at Vienna University of Economics and Business Administration. This is a revised translation of "Von Mises zu Morgenstern. Der Austroliberalismus und der Ständestaat," published in *Zeitgeschichte* 32 (2005): 323-35. A first version of this paper was written during my Schumpeter fellowship at Harvard University; the hospitality of the Weatherhead Center for International Affairs and financial support by the Joseph Schumpeter Society and the Austrian Ministry of Education is gratefully acknowledged. I thank Joachim Becker, Fritz Breuss, Harald Hagemann, Reinhard Pirker, N. Joseph Potts, and an anonymous referee for helpful comments and, in particular, Nicola Giocoli and Robert Leonard for making unpublished typescripts available to me. Of course, any remaining errors and omissions are mine. Finally, for permissions to quote from unpublished sources I am very grateful to Dorothy Morgenstern Thomas and Duke University for the papers of Oskar Morgenstern; to Bruce Caldwell, the general editor of the *Collected Works of F.A. Hayek*, for the papers of Friedrich August Hayek; to the Hoover Institution Archives for the papers of Fritz Machlup (copyright by Stanford University); to Helmut F. Furth for the correspondence of Gottfried Haberler; and to the Mises Estate and Bettina Bien Greaves for the correspondence of Ludwig Mises.

¹The term "liberal" always refers to "classical" liberalism. In the following I use capitalization to distinguish between "Austrian Economists," that is, members of the Austrian School, and "Austrian economists" for economists of Austrian origin in general, including those outside the Austrian School.

Against this background this study tries to examine the development of Austrian economics from 1934 to 1938, that is, from the end of parliamentary democracy in Austria and its replacement by the authoritarian *Ständestaat* (corporate state) regime to the eventual *Anschluss* (union) to Nazi Germany.² It starts by describing the state of the Austrian School of economics in the middle of the decade. The next section analyzes its position toward democracy and the corporate state. Then we turn to the change in leadership within the Austrian community of economists from Mises, the liberal, to Morgenstern, the technocrat, and we discuss the divergences between the strands of thought within Austrian economics as symbolized by these two men. In conclusion we sketch the fate of the Austrian School after the war.

THE OUTSET

It is useful to distinguish two strands within the Austrian School. The first is that of “Austroliberalism,” whose tradition goes back to Carl Menger and Eugen Böhm-Bawerk.³ At the beginning of the 1930s Ludwig Mises, a member of the third generation of the school, was the undisputed (if only informal) leader of this group. The most prominent among the younger members were Friedrich August Hayek, Gottfried Haberler, and Fritz Machlup.⁴ The second and less coherent strand within the Austrian School, which more closely followed the teachings of Friedrich Wieser, had a more guarded attitude toward liberalism, in theory as in practice; its best known representative was Hans Mayer, and among the younger economists Oskar Morgenstern, Alexander Gerschenkron, and Paul Rosenstein-Rodan.

It was these economists who dominated the economic discourse in Austria, at least if we restrict ourselves to economics in the more traditional sense.⁵ Besides the discussion in academic as well as journalistic writings, a vital part of this discourse was organized in a diversity of “circles” with members not only recruited from the economics profession but also from other social sciences, law, and business.⁶ Although his formal position was only that of Secretary of the Vienna Chamber of Commerce, Mises was a dominant

²On the politics and economics of the *Ständestaat* see Senft (2002); Bischof, Pelinka, and Lassner (2003); and Tälös and Neugebauer (2005).

³On the history of the Austrian School and the distinction of these two strands see Streissler (1988); Boehm (1992); and similarly Hayek (1992, pp. 42-60). The term “Austroliberalism” follows Müller (1987).

⁴Joseph Schumpeter is not included because he is typically not considered as a member of the Austrian (or any) School.

⁵We neglect, therefore, the activities of the Austromarxists and of the followers of the “romantic” tradition of “universalism.”

⁶The most important “circles” were the Mises private seminar, the so-called *Geist-Kreis* and the seminar of the Austrian Economic Society (*Nationalökonomische Gesellschaft*); see e.g., Craver (1986a, pp. 13-18) and Müller (1988, pp. 59-61).

figure in theory as well as in policy. It was at his initiative that in 1927 the Austrian Institute for Business Cycle Research was founded. Hayek was its first director (from 1927 to 1931), and Haberler was a member of the staff early on. Of the members of the Austrian School Mayer alone occupied a chair at the University of Vienna;⁷ however, as he spent most of his time on intrigues—his conflicts with Spann were notorious at the time—he exerted no lasting impact.⁸ Morgenstern, after a short spell under the influence of Spann in the 1920s, had turned soon to the Austrian tradition and worked as Mayer's assistant. After returning from a three year Rockefeller fellowship abroad, he succeeded Hayek as the director of the Institute and remained in this position until 1938.

In 1934 many of the most eminent members of the Austrian School and, in particular, of its liberal strand had left the country, due to the missing career opportunities combined with an increasing hostility toward liberals and Jews.⁹ Hayek had already in 1931 accepted a professorship at the London School of Economics, from where he advanced his international reputation as a leading representative of classical liberalism. Haberler had taught as a visiting professor at Harvard University and was now at the League of Nations in Geneva, working on his study of the business cycle (Haberler 1937). Machlup spent a two-year Rockefeller fellowship in the United States and in Great Britain. And finally, in September 1934, Mises quit his position at the Chamber and took over a professorship at the Geneva Institute of International Studies, at first only planned for a one-year term. Of the Austroliberals only the lesser known stayed in Austria, for example, Richard Strigl, Martha Stephanie Braun (one of the very few female members), and Erich Schiff.

Economically, Austria had been among the countries hit hardest by the Great Depression, and in 1934 the bottom of the slump had scarcely been overcome. From the point of view of the Austrian liberals the cause of the severity of both the crisis and the depression had to be looked for in the errors of an ill-conceived economic policy: inflationism, excessive taxes and social burdens, and rigid wages, that is in short, a violation of the whole framework of economic liberalism.¹⁰ This framework of liberal rules, as symbolized by the gold standard,¹¹ required “sound” monetary and financial policies (that

⁷The two other chairs were held by Ferdinand Degenfeld-Schönburg (an economic historian) and Othmar Spann (the founder of “universalism”).

⁸See Craver (1986a, pp. 10-13). For a more favorable evaluation of Mayer, see e.g., Ebeling (2003, pp. 2-3).

⁹On the emigration of the Austrian economists see Craver (1986a); Müller (1987); Fleck (1987), and Rathkolb (1987). For biographical information see the respective entries in Hagemann and Krohn (1999).

¹⁰On Austrian economic policy in the 1930s see Klausinger (2002).

¹¹On the “gold standard mentality” see Eichengreen and Temin (2000).

is, the avoidance of inflation¹² and of budget deficits), the freedom of international trade, and a minimum of government intervention into industry in general. To the liberals a sustainable recovery of the Austrian economy could only be accomplished by again subordinating economic policy to this framework of rules.

Politically, the time period in question was shaped by the transformation of parliamentary democracy into an authoritarian regime. The response of the Austrian Economists to this event will be examined in the next section.

THE AUSTRIAN ECONOMISTS ON DEMOCRACY AND THE STÄNDESTAAT

The sources from which to infer the position of the Austrian Economists *vis-à-vis* the corporate state are mainly twofold: First, we look into what had been written on the relation between liberalism and liberal economic policy on the one hand and the different political systems on the other hand, as e.g., in Mises (1927, 1929) or in Morgenstern (1934). Second, there are also more detailed statements on the specific situation of Austria, in particular in unpublished notes and correspondence.¹³

To begin with Mises's general treatment of liberalism, he professed himself an adherent to democracy—as opposed to a corporate state or to dictatorship—as the only political system consistent with liberalism, by its virtue of permitting nonviolent transitions of power and thereby safeguarding against civil war or revolution.¹⁴ However, he distinguished between democracy proper (that is one enlightened by the spirit of liberalism) and that kind of democracy dominated by political parties in pursuit of special interests. In particular, he was convinced that the latter kind of democracy faced the danger of being impeded in its working by the use of violence and eventually to descend into socialism. In this regard, he warned that even if democracy “is on the road to destruction . . . force is never a means of overcoming these difficulties” (Mises 1978a, p. 45). Yet, almost in the same breath and although he rejected the fascist solution for reasons of principle, he conceded “that Fascism and similar movements . . . are full of the best intentions and that their intervention has, for the moment, saved European civilization” (Mises 1978a, p. 51).¹⁵ Basically, Mises

¹²As contemporary terminology equated inflation with an increase in the (effective) quantity of money, this requirement was, in the case of growth, more stringent than a stable price level.

¹³Most of the material used is from the Fritz Machlup Papers and the Oskar Morgenstern Papers; for the sake of brevity these will be referred to by FMP and OMP, respectively. If not indicated otherwise, all translations from these and from other German-language sources are my own.

¹⁴Cf. Mises (1978a, p. 42; 1978b, p. 69).

¹⁵An anonymous referee pointed out that this quotation should be considered a mere statement of fact and not a value judgment; however, I find it difficult to interpret it otherwise than as confirming that there may be circumstances when higher-ranking goals (the “saving of civilization”) justify the abandoning of democratic principles.

identified behind the potential conflict between liberalism and (nonenlightened) democracy the more fundamental opposition of public opinion increasingly shaped by socialist ideas. As such public opinion will determine the course of events independently of the political system, whether democratic or not; in the end the mere transition to an authoritarian or corporate system will not solve the problem.¹⁶

The dilemma sketched above is to Mises paradigmatic for the Austrian situation. According to him, democracy Austrian-style had been paralyzed by the power exerted by the Social Democrats and in particular by the trade unions. For example, in one place Mises referred to the “terror apparatus . . . of the Social Democratic party” (Mises 1978b, p. 88), and he considered wage conflicts and strikes organized by trade unions as illegitimate means of violence.¹⁷ Of the other Austrians Machlup appears to have concurred with Mises’s broad diagnosis. He characterized the democratic system of Austria by the fact that the left minority prevented the conservative majority—by obstruction in parliament and mainly by the power in the streets—from effectively realizing its objectives (Machlup 1938).¹⁸ Moreover, Machlup (n.d.) maintained that if elections had been held after 1933, they would have ended with the suicide of Austrian democracy because of the majority of votes to be expected for the Austrian Nazis. Therefore, from the point of view of Mises and Machlup, probably quite typical for the Austroliberals in general, democracy Austrian style had to be considered an experiment that had failed.

The Austrians also ascribed the failure of democracy to economic aspects. The most important one was the insoluble discrepancy between the economic logic of a capitalist market economy and the improvements in social legislation, as enforced by the political power of the working class immediately after the war.¹⁹ The satisfaction of these claims for social justice were seen, in the end, as causing business losses, financial weakness, and “capital consumption,”²⁰ that is, the main causes of economic stagnation. In this regard, Hayek asked: “Can capital consumption be avoided in the long run in a democratic society in which the majority of the population is anticapitalistic?” (Hayek 1984, p. 155). In any case, the liberal recipes, a cutback in social policy to ease the burden of taxes and social duties, supplemented by wage cuts as a cost saving device, were considered as colliding with the power of organized interests within the democratic system. Thus, the Austrian Economists came to believe that within the system of Austrian democracy it would be impossible

¹⁶Cf. Mises (1978a, p. 173).

¹⁷Cf. Mises (1931, p. 17); see also Mises (2002, pp. 288-89).

¹⁸Just as the following piece, this is a typescript version of a speech.

¹⁹See, for example, retrospectively Hayek (1945).

²⁰For truly heroic attempts at estimating a quantitative measure of capital consumption in Austria see Morgenstern (1931) and Machlup (1935).

to enforce the needed liberal reforms, and indeed liberal and conservative politicians drew from this the conclusion that replacing democracy by authoritarian rule was the only way out of this dilemma.²¹

The liberals' pessimistic attitude towards the viability of Austria's democratic system did not imply a favorable view on the newly erected corporate state. For Mises it ultimately just came down to replacing one ruling group by another: "The cliché, a *Ständestaat*, . . . merely shielded the aspiration of the Christian-Social Party and its allied homeguard for complete party rule" (Mises 1978b, p. 136). Although the transition of power (to the conservatives) ensured the implementation of monetary and financial policies strictly in line with the goal of stability, conforming to the demands of the foreign creditors too, in other fields of policy the conflict of the Austrian liberals with the *Ständestaat* regime was unmistakable. They disapproved of its clerical (and somewhat disguised anti-Semitic) character,²² they complained about intellectual decay combined with progressing corruption,²³ and Max Mintz, a participant of the Mises seminars, formulated the ultimate judgment: "Never in the last 80 years has political and economic liberalism been as dead as today" (Mintz to Machlup, 9 Dec 1934. FMP, box 53, folder 25).

Another piece of evidence for the skepticism of liberal Austrian Economists toward the *Ständestaat* lies in the decision of Haberler, Machlup, and Mises not to return to their home country, but to make their emigration permanent. Haberler, on his way from Geneva to Harvard, stayed only for a short time in Vienna; Machlup withdrew his habilitation thesis, after the proceedings had been unduly delayed by the usual intrigues, liquidated his Austrian firm and accepted a chair at the University of Buffalo; and Mises extended his activity in Geneva up to 1940, when he emigrated to the United States. The correspondence between Machlup and Mises is revealing in this regard. Here Machlup referred to the Nazi question and the Jewish question as the reasons for his ultimate decision not to return to Austria.²⁴ Mises emphasized the economic aspects: "In a country where capital is consumed the whole situation is unstable" (Mises to Machlup, 23 Nov 1934. FMP, box 53, folder 27). Although they regarded the *Ständestaat* a last chance for Austria to survive as an independent state—whether through the support from the Italian fascists (Mises 1978b, p. 140)²⁵ or the restoration of the Habsburg monarchy

²¹Pronouncements in this vein are documented for Engelbert Dollfuß (the Federal Chancellor in 1934), Kurt Schuschnigg (his successor), Viktor Kienböck (the president of the Austrian central bank), and Rost van Tonningen (the representative of the League of Nations in Austria); cf. on this Kernbauer (1991, p. 389).

²²Cf. Max Mintz to Machlup, 9 Dec 1934. FMP, box 53, folder 25.

²³Cf. Hayek to Machlup, 1 May 1936. FMP, box 43, folder 15.

²⁴Cf. Machlup to Mises, 25 Sept 1934. FMP, box 53, folder 27. Both Machlup and Mises were of Jewish origin.

²⁵It should be noted that Mises's recollections were written in 1940 (and in a very pessimistic mood).

(Machlup n.d.)—the future prospects for Austria were seen as dim and the eventual *Anschluss* to the German *Reich* as almost inevitable. Significantly, Haberler already in 1936 noted the “cold nazification” of Austria (Haberler to Machlup, Aug 1936. FMP, box 41, folder 4).

Those members of the Austrian School critical of political and economic liberalism developed a friendlier attitude toward the *Ständestaat*. For example, Morgenstern propagated the idea of a “strong state” capable of overcoming the power of special interests, and in general he preferred authoritarian regimes to democracies for their capacity to implement the hard measures necessary in times of crisis.²⁶ By the way, this was a view widely shared by the (conservative) elites of the country.²⁷ In this vein, Morgenstern saw his task not in realizing an economic policy conforming to an ideal principle (as, e.g., that of liberalism), but in lending his technocratic advice for the evaluation of the possibly interventionist policy decided upon by the new government. Mayer adapted quickly to the new environment by giving a seminar on the “Economics of the corporate state,”²⁸ and another telling episode confirms his flexibility: Although he once had tried, by organizing support from Schumpeter and other German professors, to prevent the appointment of Josef Dobretsberger, a partisan of the *Ständestaat*, to a chair at the University of Graz,²⁹ he now hailed him on the occasion of his being appointed as minister of social affairs as a great scholar, comparable to his predecessor Böhm-Bawerk (Mayer 1935)—a comparison that was ill-received among the other members of the Austrian School.³⁰

Summarizing, the liberals’ judgment was more differentiated and critical as compared with the other Austrian Economists and although they accepted the end of the democratic system as unavoidable, they remained skeptical and doubted whether the *Ständestaat* would turn out to be a viable alternative.

FROM MISES TO MORGENSTERN

In this section we analyze the transformation that economics as a discipline experienced in these years in Austria, symbolized by the transition of the leadership role from Mises to Morgenstern. This section concentrates specifically

²⁶Cf. Morgenstern (1934, pp. 129–30). It is noteworthy that in the revised English version of this book (Morgenstern 1937, pp. 141–43) this statement is considerably weakened. Furthermore, the more critical position of the liberals in this regard, as of 1934, is subtly expressed in the criticism by Braun (1934, p. 23) that Morgenstern will be “much misunderstood; for he will be reproached for favoring political fascism for the sake of sound economic policies.”

²⁷See, e.g., the 1932 correspondence between Morgenstern and Viktor Brauneis (a director at the Austrian central bank), in OMP, box 4.

²⁸Cf. Machlup to Mises, 8 Apr 1935. FMP, box 53, folder 27.

²⁹Cf. Haberler to Morgenstern, n.d. [Nov 1935]. OMP, box 5.

³⁰Cf. Morgenstern to Haberler, 5 Nov 1935. OMP, box 5.

on the developments within the economics community, while the following sections examine this transformation from the point of view of theory and economic policy, respectively.

As noted above, the preconditions were favorable for Morgenstern's rise to a leading position because of the vacuum left by the emigration of the most prominent members of the Mises group, a vacuum that could not be filled by Mayer. Moreover, Morgenstern's position was furthered by some additional factors. The first and most important one was his directorship of the Institute. A Funding of the Institute by the Rockefeller Foundation³¹ had been granted from 1931 to 1935. When an attempt, undertaken jointly by Mayer, Mises, and Alfred Francis Pribram, to win the Rockefeller Foundation financing of an alternative and more comprehensive project of social science research failed,³² the funding for the Institute was extended indefinitely. Morgenstern noted in his diary: "Mises, Mayer, etc. are not going to be asked anymore" (Morgenstern diary, 26 Dec 1934. OMP, box 13). His position, now being undisputed, allowed him to extend the Institute's research beyond the narrow fields of the business cycle to more abstract topics of pure theory. Besides this, the Institute worked as a base for Morgenstern's activities as a policy advisor, which are described in more detail below. In this regard Morgenstern also succeeded in securing for the Institute a formally independent position outside Austria's expansive state bureaucracy. The role of the Institute was also relevant in another respect, as it provided employment opportunities, so rare at this time, for scientifically inclined economists outside the universities. Furthermore, Morgenstern through his contacts to the Foundation appears to have arranged for many of his collaborators at the Institute to be chosen for a Rockefeller fellowship to spend one year abroad. It is noteworthy that of the younger economists working at the Institute—Ernst John, Reinhard Kamitz, Josef Steindl, Gerhard Tintner, and Abraham Wald³³—none had a special affinity for the liberal strand of the Austrian School.

Morgenstern's activity as an editor was also important. As director of the Institute he was responsible for the *Monatsberichte* (monthly bulletins) and the *Schriftenreihe* (book series), which included contributions by Hayek, Machlup, Schiff, Morgenstern, Strigl, Nurkse, and Wald. Still more crucial was his position as the managing editor of the *Zeitschrift für Nationalökonomie*, after 1933 the only German-language economics journal with

³¹On the activities of the Rockefeller Foundation see Craver (1986b) and Leonard (2002, pp. 32–44).

³²On this episode cf. Fleck (2000).

³³Of those mentioned above Tintner, John, and Kamitz (planned for 1938/39) received stipends, but not Wald (as a stateless person of Jewish origin). By the way, the correspondence between Hayek and Machlup shows (Machlup to Hayek, 15 Feb 1934 and Hayek to Machlup, 19 Mar 1934. FMP, box 42, folder 2) that Tintner was awarded the fellowship that had been refused to the more liberally-minded Schiff.

international standing. There he used his discretion to move the journal toward a position rather critical of Austrian theory (in the tradition of Mises) while simultaneously keeping it clean of pamphlets of corporatist or fascist origin. Finally, Morgenstern regularly refereed book projects for the publisher Julius Springer in Vienna. All in all Morgenstern's influence on the publishing of economics literature in Austria was considerable.

The rise of Morgenstern corresponded to the decline of the Mises group. The absence of many of its former members led to the gradual decay of communication and debate within the diverse circles. The lectures given at the Austrian Economic Society were the exception to the rule, yet they too were no longer dominated by the Austrian liberals, neither among the speakers nor in the audience.³⁴ Similarly, the journalistic activities of the Mises group evaporated. In particular, from 1932 to 1934, the liberals had attempted to educate public opinion in the insights of Austrian Economics. For example, Machlup wrote up to 100 weekly columns, titled "*Zwei Minuten Volkswirtschaft*" ("Two Minutes of Economics") for the Viennese daily, *Neues Wiener Tagblatt*, (Klausinger 2004) and jointly with Morgenstern and some members of the Institute he supplied the same newspaper with topical comments on matters of economic policy.³⁵ Yet during 1934 all these activities stopped, on the one hand because of Machlup's emigration, and on the other hand because of the decreasing interest in lectures in liberalism combined with the interventions of censorship: "On the most important topics I must not write, and to write on unimportant topics is not worthwhile" (Machlup to Dr. Hugo Glaser [of the *Neues Wiener Tagblatt*], 6 Apr 1934. FMP, box 55, folder 18).³⁶ Finally, a look at the Austrian universities confirms the above picture. Vacant chairs were filled up with adherents to the new regime, like Dobretsberger in Graz and Richard Kerschagl at the *Hochschule für Welthandel* in Vienna, and Morgenstern received the honorary title of "extraordinary professor." In contrast, the remaining Austrian liberals had to content themselves with secondary roles outside academia, and in general the flow of emigration of Austrian economists remained steady.³⁷

³⁴The loss of this center of communication might have caused the increasing divergence of the theoretical positions held within the Austrian School in the 1930s. For a closer examination see Klausinger (2006).

³⁵See *Neues Wiener Tagblatt* to Morgenstern, n.d. [Jan 1932]. OMP, box 6, and Morgenstern to Grätz, 4 Apr 1932. OMP, box 5. Most of these commentaries are reprinted in Machlup et al. (2005).

³⁶On the problems with censorship see also Morgenstern to Machlup, 19 and 26 Mar 1934. FMP, box 54, folder 15.

³⁷Thus, in 1936 Rosenstein-Rodan took a permanent position at the University College in London, Tintner left in 1937 for Iowa State University, and Karl Menger taught as a visiting professor at Notre Dame in 1937/38.

Therefore, insofar as the Austrian School kept its influence intact even during the *Ständestaat* regime, it was now no longer represented by the members of the liberal strand but instead by the followers of Morgenstern (and to some extent Mayer).

FROM APRIORISM TO EXACT THEORY

Yet, the transition of the leading position from Mises to Morgenstern was more significant than just an exchange of persons, for it brought to light diverging theoretical positions. In fact, as we shall see, the more Morgenstern acquired the leadership within the Austrian community of economists, the less did he still consider himself (and was considered by others) an Austrian Economist.

In the 1930s Morgenstern attempted to formulate an independent theoretical position critical of the approach of Mises and Hayek—thereby questioning the leadership of Mises as well as the principally liberal orientation of Austrian Economics. As early as 1933 he wrote: “For the Viennese it is not unimportant that it is realized in Germany that the common impression as if Mises were the leader of the local economics community and all the other economists, especially the younger ones, looked up at him, does not correspond to the facts” (Morgenstern to Vleugels, 6 May 1933. OMP, box 7). However, his endeavor for autonomy was characterized by the combination of his harsh criticism of the state of contemporary economic theory and his attempts at revolutionary alternatives that were at best sketchy and sometimes confused.³⁸

In any case, in the debates between Morgenstern and the Austrian School various levels of conflict can be distinguished. First, their views on the foundations of economic policy were opposed to each other. In this regard, Mises adhered to the thesis that the superiority of economic liberalism could be derived from the propositions of economic theory, based on aprioristic foundations:

[T]he science of economics proves with cold, irrefutable logic that the ideals of those who condemn making a living on the market are quite vain, that the socialist organization of society is unrealizable, that the interventionist social order is nonsensical and contrary to the ends at which it aims, and that therefore the market economy is the only feasible system of social cooperation. (Mises 1960, p. 196)

Morgenstern, in contrast, considered liberalism (and socialism) as examples of “rigid systems of economic policy” that cannot be justified by the insights of economic theory.³⁹ Instead he insisted that policy advice should be purely

³⁸Haberler, a personal friend of Morgenstern, remained skeptical: “Your *sweeping condemnations* of all possible people are very amusing. However, they put a heavy burden of responsibility on your forthcoming works” (Haberler to Morgenstern, 15 Aug 1934. OMP, box 5; the italicized phrase is English in the original).

³⁹Cf. Morgenstern (1934, chap. 3).

technocratic, i.e., free of value judgments, so that in his view the economist as a policy advisor had to accept the goals as they resulted from the political process (Morgenstern 1934, pp. 4 and 9).⁴⁰ Consequently, his theory of economic policy was compatible with a policy of interventionism, which Mises had strictly rejected. Of course, Morgenstern's hostility toward the Mises approach, although somewhat veiled, did not go unnoticed and caused a chilly reception among the liberals—for example, Hayek characterized Morgenstern's book as “mean-spirited and yet impertinent in its tone” (Hayek to Machlup, 14 Jan 1934. FMP, box 42, folder 2).⁴¹

The second level of dispute arose from questions of methodology. As already noted, Mises and to some extent his followers⁴² relied on aprioristic foundations for economics as a science of action, i.e., of “praxeology,” while Morgenstern held that economic theories should rest on an “exact” basis and their validity be determined on empirical grounds. Thereby “exactness” meant an axiomatic-mathematical foundation of economic theory⁴³ free of (liberal) value judgments—whereas the antiformalistic position of the other Austrians (from Mises to Mayer) rejected the use of mathematical tools. Although Morgenstern in the 1930s failed in his own attempts to develop such an “exact” foundation for economics—a planned book on time and economic equilibrium⁴⁴ never went beyond a mere expression of intent—the lack of exact thinking was an ever present argument by which he reproached all his Austrian rivals. An article by Hayek appeared to Morgenstern as “a model of confusion” (Morgenstern diary, 3 Sep 1935. OMP, box 13), on the occasion of Karl Menger's lecture on the law of returns⁴⁵ he noted that Haberler was “far from understanding the fundamentals of these exact things [and] Mises talked pure

⁴⁰Morgenstern (1934, p. 57) illustrated his position by an example where free trade is excluded as an option because policy-makers have decided to protect an important group of the population from foreign competition.

⁴¹In his correspondence with Morgenstern Hayek's reaction was more diplomatic, yet still unambiguous; moreover he complained that “you . . . were rather rude to some of my friends” (Hayek to Morgenstern, 2 Apr 1934. OMP, box 5). See also the critical review by Braun (1934).

⁴²Haberler and Hayek eventually turned away from Mises's position. See Haberler (1933, p. 94) and Hayek (1937).

⁴³See Morgenstern (1936a). Undoubtedly Morgenstern's methodological position was shaped by his participation in two more of the Viennese circles, the Vienna circle of the philosophers around Moritz Schlick and the “Mathematical Colloquium” initiated by Karl Menger, the son of the founder of the Austrian School. On the importance of these circles for modern economic theory see Giocoli (2003, pp. 230–42) and Weintraub (1985, pp. 62–80).

⁴⁴Cf. Morgenstern diary, 4 Nov 1934. OMP, box 13.

⁴⁵Later to be published, jointly with Morgenstern (1936a), in the *Zeitschrift* as Menger (1936), on the occasion of which Hayek noted: “The Morgenstern-Menger group and thereby the *Zeitschrift* commit terrible things scientifically” (Hayek to Machlup, 1 May 1936. FMP, box 42, folder 2).

nonsense” (ibid., 31 Dec 1935. OMP, box 14), and his advice to Machlup was: “If only he would finally begin doing *science*” (ibid., 27 Oct 1935. OMP, box 14; emphasis in the original).

Finally, on a third level, there was also disagreement with regard to the basic tenets that constituted Austrian Economics. This can be most easily seen by looking at the three major controversies in which Austrian Economics had become involved in the 1930s, that is, the controversy on the nature of capital, on the possibility of economic calculation in socialism, and—in the debate with Keynes and his followers—on business cycle theory and policy.⁴⁶ Significantly, Morgenstern remained silent on the economic calculation debate, and he strictly opposed Austrian capital theory as derived from Böhm-Bawerk, with its emphasis on the time dimension of capital.⁴⁷ In his view of the business cycle Morgenstern’s position towards Austrian theory, as put forward by Mises and Hayek, appears as rather ambiguous. For he concurred with the Austrians in their adherence to the gold standard mentality and therefore in the rejection of Keynesian ideas designed to combat the depression by expansionist policy.⁴⁸ Yet he objected to central concepts of Austrian business cycle theory such as, for example, the “natural rate of interest,” which he considered a “mystical affair” (Morgenstern 1976a, p. 402 and 1936a, p. 20).⁴⁹ In a sense Morgenstern contented himself with justifying “sound” monetary and financial policies by the eclectic proposition, supported by conventional wisdom, of the crisis being the inevitable consequence of preceding inflationary excesses.⁵⁰

In sum, it is evident that Morgenstern’s rise to leadership within the economics community of the *Ständestaat* meant a turn-away from the positions of Austrian liberalism and, with regard to the Institute, a reorientation of the fields of research. However, the revolutionary critique of current economic theory that he strived for had to wait for its formulation until the time of his cooperation with John von Neumann.⁵¹

⁴⁶On the Austrians’ apparent defeat in these controversies see Caldwell (1988, pp. 517–21) and Blaug (1992).

⁴⁷See Morgenstern (1935).

⁴⁸See on this Klausinger (2002, pp. 15–21).

⁴⁹For his critique of “neutral money” see Morgenstern to Knight, 12 Sep 1934. OMP, box 6.

⁵⁰Morgenstern’s writings on the business cycle lacked originality. As evidence see the typescript of a lecture, the “Konjunktur-Vortrag,” Jan 1936. OMP, box 26.

⁵¹For Morgenstern’s development in the 1930s as a precursor of game theory see Rellstab (1991) and Leonard (1995).

FROM LIBERALISM TO PRAGMATISM

Until 1934 the impact of Austroliberalism in the Austrian economic policy debate had been considerable. Mises's position as the Secretary of the Vienna Chamber of Commerce offered him the possibility to directly influence the process of policy decision-making by his proposals and programs. Moreover, as noted above, the liberals—with the then still united journalistic efforts of Mises, Machlup, and Morgenstern—tried to create a climate favorable to economic liberalism. Yet, this ended when after Morgenstern's appointment as director of the Institute and Mises's emigration to Geneva Morgenstern became one of the most important policy advisors to the authoritarian government.

Morgenstern's activities as a policy advisor were manifold. He held a number of formal positions within the Austrian bureaucracy, for example, as an advisor to the Ministry of Commerce, where he was responsible for questions of traffic infrastructure and in particular for the Austrian railroads; as a member of the inter-ministry commission that regulated commodity prices, mainly of agricultural products; and as a representative of the Austrian government at international conferences, at the League of Nations, and at the negotiations with foreign debtors after the 1931 banking crisis. Sometimes Morgenstern's informal relations, among others with Kienböck, the President of the Austrian central bank, and with the Ministry of Finance, in particular with Ludwig Draxler, the architect of an austerity course in financial policy (from October 1935 to November 1936), were still more important. During this period Morgenstern produced a series of memoranda, some of which subsequently were made public.⁵²

Morgenstern also integrated his activities in policy advice with his directorship of the Institute, which once led the Rockefeller Foundation, responsible for most of the funding, to doubt its independence from the government. In a telling episode Tintner, who had worked for the Institute and at this time had already left Austria for the United States, reported to the Foundation that Morgenstern tried to avoid any critical review of government policies (especially in the *Monatsberichte*) in exchange for having a free hand in his internal role as an advisor.⁵³ Obviously, Morgenstern succeeded in dispelling this suspicion,⁵⁴ and the funding from the Foundation continued unabated. Yet, a glance at the *Monatsberichte* confirms that the comments on government policies were exceedingly restrained and nonspecific;⁵⁵ and even in 1938 Morgenstern (then

⁵²See, for example, Morgenstern (1936b and 1936c).

⁵³Cf. Leonard (2002, pp. 38-39).

⁵⁴In a letter to John, Morgenstern accused Tintner of a pathological hatred against anything of Austrian origin, see Morgenstern to John, 6 Jul 1937. OMP, box 5.

⁵⁵This tameness (and Morgenstern's turning away from the Mises group) might explain the fact, emphasized by Rosner (1999, pp. 221-22), that the business cycle analyses in the *Monatsberichte* are often in contradiction to the Mises-Hayek theory.

already in the United States) and Kamitz were eager to censor a contribution that was too favorable towards a policy of public works.⁵⁶

For Morgenstern's role as a policy advisor 1936 became the crucial turning point. Then, after the eventual breakdown of the Gold bloc and the devaluation of the currencies of its member countries (France, Switzerland, and the Netherlands) Austria had to decide whether to devalue the Austrian schilling too or to stabilize the current parity.⁵⁷ As the control of Austrian economic policies (by the League of Nations and the foreign creditors) had already been considerably eased, Austrian policy could decide on this issue autonomously. In conformity with Morgenstern's recommendations, the Austrian government opted for a stable currency.

Two aspects of this decision are remarkable. On the one hand, Morgenstern's orthodox advice was not based on a specific economic theory and, in particular, not based on the Austrian view of the business cycle, and he was rather astonished that "all the 'foreigners' are ever asking, why we did not devalue" (Morgenstern diary, 24 Jul 1937, OMP, box 13).⁵⁸ On the other hand, Morgenstern's recommendation for stabilizing the currency had been conditioned on a supplementary policy of lowering prices, directly by means of the already existing price controls (primarily directed at agricultural products) and indirectly by opening up some industries to international competition.⁵⁹ However, this policy of lowering prices failed because it was opposed by the very special interests on whose support the government relied.

Morgenstern's recommendations for trade and industrial policy suffered a similar fate. Although he—unlike the liberals—was convinced of the necessity to regulate markets in the face of economic power, conflicts of interest, and monopolization, he regarded the current scheme of "market regulation" (*Marktordnung*) as highly inefficient and pleaded for an easing of those regulations (*Auflockerung*).⁶⁰ When his hopes to influence economic policy for the better were disappointed in this regard too, he abandoned his political activities and started to concentrate again on his scientific career. In January 1938 he left Austria for a three-month visit to American universities. In retrospect and after the *Anschluss* the economic policies of the *Ständestaat* became the subject of a devastating critique—they should be relegated to that "great field . . . which might appropriately be called the 'pathology of economic policy'" (Morgenstern 1939, p. 39).

⁵⁶See on this Steindl (1988, p. 400).

⁵⁷For a more extensive discussion see Klausinger (2002, sec. 6).

⁵⁸One of those "foreigners" was Haberler, who argued his position in no less than four letters (see Haberler to Morgenstern, 30 Oct, 20 Nov 1936, 9 Jan 1937, and n.d. [1937]. OMP, box 5) and already earlier had advised to follow a devaluation of the gold bloc currencies (17 Jul 1934. OMP, box 5).

⁵⁹See Morgenstern (1936c, p. 169).

⁶⁰See *ibid.*

Thus, in these years thanks to Morgenstern the Austroliberals' approach to economic policy and policy advice had been replaced by a more pragmatic (or technocratic) position. It is the more remarkable that this did not imply a policy change in the fields of monetary and financial policies, where the rule of the gold standard mentality continued more or less unquestioned. However, in other fields, like those of trade and industrial policy, where Morgenstern's suggestions (of a cautious policy of easing regulations) collided with the organized interests of the *Ständestaat*, economic reasoning was defeated by political necessities—thus in some respect confirming the “limits of economic policy” to which Morgenstern had alluded in his book. It was these limits (and not Austria's eventual *Anschluss* to Nazi Germany) that ended Morgenstern's career as a policy advisor to the Austrian government.

EPILOGUE

The *Anschluss* marked the final exodus of the Austrian School from its country of origin. Many Austrian economists desperately seized the last opportunity to escape the Nazi occupation, among them most of the Austrian liberals, and Steindl and Wald of the above mentioned members of the Institute; Karl Schlesinger committed suicide. Henceforth the Austrian School existed only outside Austria and in a state near to dissolution—lacking the networks of communication typical of the Austrian (and Viennese) economics community and under siege from a “new economics” hostile toward classical liberalism. Up until Hayek's 1974 Nobel prize Austrian economics survived only in the various Mises circles, primarily in the United States, and even since then radical-liberal neo-Austrian economics does not amount to more than a marginalized faction of the mainstream of economic theory.

For Morgenstern, who had just completed his tour as a visiting professor in the United States, the *Anschluss* meant his dismissal as the director of the Institute. The Institute came under the supervision of the German Ernst Wagemann, and of Morgenstern's co-workers only Kamitz and John stayed, earning them the belated accusation of having been “Nazis” (Morgenstern 1976b, p. 807); all the others were suspended or had already left Austria in time. Morgenstern was appointed to Princeton University, where his collaboration with von Neumann marked the climax of his scientific work and his career. In the first chapter of the jointly authored work on game theory (von Neumann and Morgenstern 1944) Morgenstern finally succeeded in summing up his critique of contemporary economic theory—and it may be considered an irony that after half a century, game theory presently finds itself at the very core of mainstream economic theory. Anyway, Morgenstern's later scientific work did not show any affinity whatsoever to that of the Austrian School.

In Austria Mayer demonstrated his flexibility by dismissing all non-Aryan members from the Austrian Economic Society.⁶¹ Thanks to his (lack

⁶¹See Mises (1978b, p. 99).

of) reputation the nonliberal strand of the Austrian School soon fell into oblivion, although he possibly considered himself the last Austrian Economist at the University of Vienna. Or as Mises put it: “Mayer is as always in floribus,” probably still pretending to be an Austrian Economist.⁶²

REFERENCES

- Bischof, Günter, Anton Pelinka, and Alexander Lassner, eds. 2003. “The Dollfuss/Schuschnigg Era in Austria. A Reassessment.” *Contemporary Austrian Studies* 11.
- Blaug, Mark. 1992. “Commentary” [on Boehm]. In Caldwell and Boehm, eds. 1992. Pp. 31-34.
- Boehm, Stephan. 1992. “Austrian Economics Between the Wars: Some Historiographical Problems.” In Caldwell and Boehm, eds. 1992. Pp. 1-30.
- Braun, Martha Stefanie. 1934. Review of Oskar Morgenstern, “Die Grenzen der Wirtschafts-politik.” *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 16: 21-23.
- Caldwell, Bruce J. 1988. “Hayek’s Transformation.” *History of Political Economy* 20: 513-41.
- Caldwell, Bruce J., and Stephan Boehm, eds. 1992. *Austrian Economics: Tensions and New Directions*. Boston-Dordrecht-London: Kluwer.
- Craver, Earlene. 1986a. “The Emigration of the Austrian Economists.” *History of Political Economy* 18: 1-32.
- . 1986b. “Patronage and the Directions of Research in Economics: The Rockefeller Foundation in Europe, 1924-1938.” *Minerva* 24: 205-22.
- Ebeling, Richard M. 2003. *Austrian Economics and the Political Economy of Freedom*. Cheltenham-Northampton, U.K.: Edward Elgar.
- Eichengreen, Barry, and Peter Temin 2000. “The Gold Standard and the Great Depression.” *Contemporary European History* 9: 183-207.
- Fleck, Christian. 2000. “Die gescheiterte Gründung eines Zentrums für sozialwissenschaftliche Forschung in den 30er-Jahren in Wien.” *Archiv fuer die Geschichte der Soziologie in Oesterreich-Newsletter* 20: 15-29.
- . 1987. “Rückkehr unerwünscht. Der Weg der österreichischen Sozialforschung ins Exil.” In Stadler, ed. 1987. Pp. 182-213.
- Giocoli, Nicola 2003. *Modeling Rational Agents. From Interwar Economics to Early Modern Game Theory*. Cheltenham-Lyme, U.K.: Edward Elgar.
- Haberler, Gottfried. Papers. Hoover Institution Archives. Stanford University.
- . 1937. *Prosperity and Depression: A Theoretical Analysis of Cyclical Movements*. Geneva: League of Nations.

⁶²Mises to Hayek, 8 Dec 1945. Friedrich August Hayek Papers (Hoover Institution Archives, Stanford University), box 38 (English in the original).

- . 1933. "Der Stand und die nächste Zukunft der Konjunkturforschung." In *Festschrift für Arthur Spiethoff*, G. Clausing, ed. München: Duncker and Humblot. Pp. 92-103.
- Hagemann, Harald, and Claus-Dieter Krohn, eds. 1999. *Biographisches Handbuch der deutschsprachigen Wirtschaftswissenschaftlichen Emigration nach 1933*. München: Saur.
- Hayek, Friedrich A. Papers. Hoover Institution Archives. Stanford University.
- . 1992. *The Fortunes of Liberalism*. Vol. 4: *The Collected Works of F.A. Hayek*. Peter G. Klein, ed. London: Routledge.
- . 1984. *Money, Capital, and Fluctuations. Early Essays*, Roy McCloughry, ed. London: Routledge and Kegan Paul.
- . 1945. "The Future of Austria." *The Spectator*, 6 Apr; as reprinted in Hayek 1992, pp. 234-36.
- . 1937. "Economics and Knowledge." *Economica* 4: 33-54.
- . 1932. "Kapitalaufzehrung." *Weltwirtschaftliches Archiv* 36: 86-108. Translation in Hayek. 1984, pp. 136-58.
- Kernbauer, Hans. 1991. *Währungspolitik in der Zwischenkriegszeit. Geschichte der Oester-rei-chi-schen Nationalbank von 1923 bis 1938*. Vienna: Oesterreichische Nationalbank.
- Klausinger, Hansjörg. 2006. "In the Wilderness." Emigration and the Decline of the Austrian School. Forthcoming in *History of Political Economy* 38.
- . 2004. "Two minutes of Austrian economics." Fritz Machlup's journalistic writings, 1932-1934. *Research in the History of Economic Thought and Methodology* 22-B, 97-130.
- . 2002. The Austrian School of Economics and the Gold Standard Mentality in Austrian Economic Policy in the 1930s. Working Paper, Center for Austrian Studies at the University of Minnesota.
- Leonard, Robert. 2002. "Risk, Foresight-Flight." Morgenstern's Vienna in the 1930s. Working Paper, University of Quebec at Montreal.
- . 1995. "From Parlor Games to Social Science: von Neumann, Morgenstern, and the Creation of Game Theory 1928-1944." *Journal of Economic Literature* 33: 730-61.
- Machlup, Fritz. Papers. Hoover Institution Archives. Stanford University.
- . 1938. Political Situation of Austria. Machlup Papers, box 86, folder 43.
- . 1935. "The consumption of capital in Austria." *Review of Economic Statistics* 17: 13-19.
- . n.d. Austria as the Pawn of Europe. Machlup Papers, box 86, folder 40.
- Machlup, Fritz, Oskar Morgenstern, Gottfried Haberler, F.A. Hayek et al. 2005. *Wirtschaftspublizistische Beiträge in kritischer Zeit, 1931-34*. Edited by H. Klausinger. Marburg: Metropolis.
- Mayer, Hans. 1935. "Ein Mann der Wissenschaft im Sozialministerium." *Wiener Zeitung* (3 November).
- Menger, Karl. 1936. "Bemerkungen zu den Ertragsgesetzen." *Zeitschrift für Nationalökonomie* 7: 25-56.

- Mises, Ludwig von. 2002. *Between the Two World Wars: Monetary Disorder, Interventionism, Socialism, and the Great Depression. Selected Writings of Ludwig von Mises*. Vol. 2. Richard M. Ebeling, ed. Indianapolis: Liberty Fund.
- . [1927] 1978a. *Liberalism: A Socio-Economic Exposition*. Kansas City: Sheed Andrews and McMeel.
- . 1978b. *Notes and Recollections*. Spring Mills, Penn.: Libertarian Press.
- . [1933] 1960. *Epistemological Problems of Economics*. Princeton, N.J.: Van Nostrand.
- . 1935. "Der Weg der österreichischen Finanzpolitik. Rückblick und Ausblick." *Wirtschaftliche Nachrichten* 18 (1): 38-39. Translation in Mises. 2002. Pp. 286-93.
- . 1933. *Grundprobleme der Nationalökonomie*. Jena: Gustav Fischer.
- . 1931. *Die Ursachen der Wirtschaftskrise*. Tübingen: Mohr.
- . 1929. *Kritik des Interventionismus*. Jena: Gustav Fischer.
- . 1927. *Liberalismus*. Jena: Gustav Fischer.
- Morgenstern, Oskar. Papers. Special Collections Library. Duke University.
- . 1976a. *Selected Economic Writings of Oskar Morgenstern*. Andrew Schotter, ed. New York: New York University Press.
- . 1976b. "The Collaboration Between Oskar Morgenstern and John von Neumann on the Theory of Games." *Journal of Economic Literature* 14: 805-16.
- . 1939. "The Experience with Public Regulation and Public Monopoly Abroad." In "Monopoly and Competition in Industry and Labor," J.A. Krout, ed. *Proceedings of the Academy of Political Science* 18 (2): 34-39.
- . 1937. *The Limits of Economics*. London: William Hodge. Rev. trans. of Morgenstern 1934.
- . 1936a. "Logistik und Sozialwissenschaft." *Zeitschrift für Nationalökonomie* 7: 1-24. Translation in Morgenstern 1976a. Pp. 389-404.
- . 1936b. "Die Einordnung der Verkehrspolitik in die allgemeine Wirtschaftspolitik." *Mitteilungen des Verbandes der österreichischen Banken und Bankiers* 18 (1/2): 11-23.
- . 1936c. "Währung und Preise." *Österreichische Zeitschrift für Bankwesen* 1: 166-71.
- . 1935. "Zur Theorie der Produktionsperiode." *Zeitschrift für Nationalökonomie* 6: 196-208.
- . 1934. *Die Grenzen der Wirtschaftspolitik*. Vienna: Julius Springer.
- . 1931. "Kapital- und Kurswertänderungen der an der Wiener Börse notierten Aktiengesellschaften 1913 bis 1930." *Zeitschrift für Nationalökonomie* 3: 251-55.
- Müller, Karl H. 1988. "Hochzeit der Sozialwissenschaften 1871-1938." In *Geschichte der österreichischen Soziologie*. J. Langer, ed. Vienna: Verlag für Gesellschaftskritik. Pp. 51-69.
- . 1987. Die Idealwelten der österreichischen Nationalökonomien. In Stadler, ed. 1987. Pp. 238-75.
- Rathkolb, Oliver. 1987. "Überlegungen zum Exodus der 'Jurisprudenz.'" In Stadler, ed. 1987. Pp. 276-303.
- Rellstab, Urs. 1991. *Ökonomie und Spiele. Die Entstehungsgeschichte der Spieltheorie aus dem Blickwinkel des Ökonomen Oskar Morgenstern*. Chur: Rüegger.

- Rosner, Peter. 1999. "The Austrian Research on Business Cycles." *History of Economic Ideas* 7: 195-226.
- Senft, Gerhard. 2002. *Im Vorfeld der Katastrophe. Die Wirtschaftspolitik des Ständestaates, Österreich 1934-1938*. Vienna: Braumüller.
- Stadler, Friedrich, ed. 1987. *Vertriebene Vernunft I: Emigration und Exil Österreichischer Wissenschaft 1930-1940*. Vienna: Jugend und Volk.
- Steindl, Josef. 1988. "Zeitzeuge." In *Vertriebene Vernunft II: Emigration und Exil Österreichischer Wissenschaft*. F. Stadler, ed. Vienna: Jugend und Volk. Pp. 399-401.
- Streissler, Erich. 1988. "The Intellectual and Political Impact of the Austrian School of Economics." *History of European Ideas* 9: 191-204.
- Talos, Emmerich, and Wolfgang Neugebauer, eds. 2005. "Austrofaschismus." *Politik—Ökonomie—Kultur 1933-1938*. 5th rev. ed. Münster: Lit Verlag.
- Von Neumann, John, and Oskar Morgenstern. 1944. *The Theory of Games and Economic Behavior*. Princeton, N.J.: Princeton University Press.
- Weintraub, E. Roy. 1985. *General Equilibrium Analysis. Studies in Appraisal*. Cambridge: Cambridge University Press.

