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## **Carl Menger on States as Orders, Not Organizations: entangled economy into a neo-Mengerian approach**

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### **Abstract.**

My contribute deals with the link between Wagner's entangled political economy and Carl Menger's economic thought. It is mainly based on what Wagner himself has called "neo-Mengerianism": a new approach that considers economics as a discipline focused on the network-based interrelations among phenomena (based on human decisions) and political economy as embedded in a social framework no longer neutral from a political point of view.

**Keywords:** Neo-Mengerianism, emergentism, biology, social needs.

**JEL Classification:** B13; B31; B53

*[H]uman economy and property have a joint economic origin since both have, as the ultimate reason for their existence, the fact that goods exist whose available quantities are smaller than the requirements of men. Property, therefore, like human economy, is not an arbitrary invention but rather the only practically possible solution of th[at] problem.*

Menger 1871

*A national economy is a complex organism of economies, but it is not itself an economy (...) National economy is a multiplicity of economics joined together into a higher unity which is nevertheless not an economy itself in the strict meaning of the word*

Menger 1883

*Money has not been generated by law. In its origin it is a social, and not a state institution. Sanction by the authority of the state is a notion alien to it. On the other hand, however, by state recognition and state regulation, this social institution of money has been perfected and adjusted to the manifold and varying needs of an evolving commerce, just as customary rights have been perfected and adjusted by statute law.*

Menger, 1892

*The 'needs of human associations'[are] common needs shared by individuals who are voluntary linked in a particular association, able to provide common goods required by the members of that association. As soon as they arise, they are no longer the sum of single individuals, and they cease to be merely means to satisfy common needs: they acquire their own needs, and social goods are required to satisfy them.*

Menger 1923

## **Introduction**

Wagner's work is based on the too often forgotten fact that economics, or better said political economy, had been emerged as a part of humanities within the history of social sciences: Adam Smith as well as other Founder Fathers, was a professor of moral philosophy. The initial aim of political economy was to understand why some societies flourish while others stagnate. As it is well known during the last century, a massive introduction of formalism and the import of physics into the methodological framework of political economy led the discipline to struggle for its own scientific status. The transformation of political economy into economic science (economics) led the discipline to forget any fruitful interaction and interconnection with the other social sciences.

During the last few years, Wagner has been proposing to replace economics as regarded by mainstream economists with a new form political economy, which he named "entangled economy". In Wagner's entangled economy, political institutions as well as economic ones are no longer performing uniquely on efficiency: their mutual interaction is much more complex than a linear function has the ability to be maximized. For instance, according to Wagner, both State and market "describe a process of interaction among participants and not some coherent set

of optimizing choices” (Wagner 2010, 160). This new way of considering institutions is able to re-build the forgotten tie between economics and the other social sciences.

Wagner considers Carl Menger as a forerunner of his approach. Wagner suggests a new way of reading Menger’s work to the history of economics and he suggests a “neo-Mengerian” approach, where entangled political economy would be rooted. Menger’s vision of society as a complex organism, not reducible to some average or representative individual is the starting point for what Wagner has in mind: (1) a new approach that considers economics as a discipline focused on the network-based interrelations among phenomena, specifically based on human decisions, and (2) economics as necessarily embedded in a social framework and no longer neutral from a political point of view (Wagner 2007).

A possible interpretation of Menger’s thought through the notion of entangled economy is fascinating. The aim of this paper is to go one step further on Wagner’s interpretive reading of Menger by introducing the second edition of Menger’s *Principles* (1923) in order to strengthen this interpretation. Although the still unavailable translation into English of the second edition of Menger’s *Principles* makes things more complicated, the possibility to show a sort of entangled political economy in Menger’s works is both challenging and definitely possible. Wagner developed his concepts by considering Menger’s first edition of his *Principles* (1871) as well as Menger’s book on methodology (1883).

In the second edition of his *Principles*, Menger described economic activity as a complex biological development of the human species and he reconsidered the role of institutions (basically the State, but also money) as orders and not as organizations (Polanyi 1971, Yagi 1993, Cangiani 2006, Ikeda 2008, Becchio 2011). There are two parts where the reader can

recognize an entangled political economy approach: (1) the role of biology to explain economic activity, (2) the nature of “social groups” as “orders” and “not organizations”. In this passage Menger introduced a shift from his original individualism to a new approach that considers the active and ineludible role of social institutions (including the State) in economic activity.

### **1. From biology to economy in Menger 1923**

Menger had never considered economy as a model where equilibrium can be reached: he regarded economy as an open system based on multiple dynamics amongst individuals and between them and their environment (the so-called Mengerian organicism). In his latest work (1923), he explicitly introduced biology to explain the origin of the economy: namely, he discussed the relation between the subject (individuals) and the object (individual choices to achieve an economic good) of economy, by stating the importance of understanding how cerebral forms of learning are working, and how they are influenced by the environment where subjects are living<sup>1</sup>. If an individual is located in a particular eco-system, the only way to understand the mechanism of their knowledge (that will lead to an economic choice) is to consider actions, interactions, and feedback as emerging forms emanating from the external environment.

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<sup>1</sup> Modern biology has passed from the romantic concept of ‘organicism’ to the modern concept of ‘organizationalism’: if organism and organizations are considered complementary and isomorphic, their functions can be described as a whole in terms of the theory of self-organizations. In 1945, Schrödinger showed that living organizations don’t obey the second thermodynamic principle and later von Neumann pointed out the differences between living machines (self-organized systems) and artificial machines (simply organized systems) (von Neumann 1966).

Adopting the concept of emergentism<sup>2</sup> developed the rejection of a sharp dualism in the social sciences. John Stuart Mill was the first philosopher who used the term in order to explain some properties of dynamics of some physical and social realities, (Mill 1843)<sup>3</sup>. Menger often quoted Mill; Menger had already explained the distinction between some social planned phenomena (legislation) and some other social unintended phenomena (money and language), to be intended as the results of a spontaneous emergence as outlined in his methodological book (1883). In fact he wrote, “the problem which science has to solve consists in the explanation of a social phenomenon of a homogeneous way of acting on the part of the members of a community” (...) “the general nature of the process to which those social phenomena owe the origin which are not the result of socially teleological factors, but are the unintended result of social movement” [Menger 1883, 152; 158].

As it is well recognized, this way of describing social facts (including economy) was carried out by Menger in a strong opposition to Gustav Schmoller, who supported a historical point of view,

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<sup>2</sup> From a methodological point of view, many economists evoked the concept of emergence as compatible with individualism: they “invert[s] the causal arrow of the structural determinists: instead of top-down causation, [and] focus on bottom-up causation, which they often refer to as emergence” (Sawyer 2005, 195). Against this kind of position, Israel proposed a different approach to the epistemological status of the science of complexity (Israel 2005). He claimed that the hope of superseding reductionism by means such as “emergence” is fallacious, because science of complexity proposes forms of reductionism even more restrictive than the classical ones. Israel is strongly adverse to the notion of complexity because of the absence of any rigorous definition.

<sup>3</sup> A modern concept of emergentism is due to the General System Theory by Ludwig von Bertalanffy (Bertalanffy 1950). From a historical point of view, its forerunners were the XIX century Darwinian organicists like Schäffle and Spencer. In 1938, Ablowitz defined “emergence” as a non-addictive, non-predictable or deductible, hierarchical element: “the essential newness of the theory itself lies in its emphasis on unpredictability, for in no previous philosophy has this concept been so central: it is thus a kind of philosophical analogue to the Heisenberg principle of uncertainty in the behavior of electrons” (Ablowitz 1938 p.12). And, being aware of the possible “mystical” development of the application of emergence, he added: “however, like alcohol, it is stimulant only in proper doses: many who have used it have gotten drunk in the attempt to apply it to everything” (ibid, p.16).

according to which social phenomena are historically determined and cannot follow in any regularity, much like natural phenomena. Menger, who supported a possible analogy between some social phenomena and natural organisms, delved further on this aspect in his latest work: before dealing with how to get resources in a context of scarcity, economy is a research on how some human needs arise. Moreover he stated that a theory of human needs (i.e., how a need arises in human minds) bridges the gap between biology and economic theory (i.e., how an individual is able to get an economic good to satisfy their original need): “the needs inherent in human nature are the starting point of any economic inquiry. ... The theory of human needs (the knowledge and understanding of their nature) is of fundamental importance for economic science .” (Menger 1923, 1).

At that time Menger had neither instruments nor applicable data that would enable him to explain how neurological mechanisms worked in the human brain. Nonetheless, he clearly intuited that biological changes in human minds due to an increase of a need represent the starting point of an inquiry into the nature of economy.

Menger went continued on: he introduced the idea that biological impulses are determined by the interaction between individuals and their natural environment. He underlined how many similar mechanisms of biological feedback between humans and their environment are shared among many animals. Interestingly, human beings and some other animal species have similar social dynamics that enable a rational organization of social life: economy is the highest rational form to organize social life, henceforth economic activity is grounded on biological structures.

The central role of environment in the changes of species, as well as the tendency of organisms to become more and more complex, were Lamarck’s theoretically ideas. Although Lamarck’s

concepts on animal evolution have been discredited later, they were adopted by Menger through Schäffle (Streissler 1990)<sup>4</sup>. On one hand, they are compatible with the classical cause-effect explanation previously adopted by Menger, and, on the other hand, they would have allowed Menger to find a general description of how brains work when humans and animals are affected by an external stimulus. Another fundamental idea in Lamarck, i.e., the spontaneous generation of more complex living forms from the simplest ones, is compatible with the Mengerian idea of spontaneous order in describing the origins of institutions<sup>5</sup>. Incidentally, on this issue, the connection between Menger and Herbert Spencer's idea of super-organic evolution seems to be plausible<sup>6</sup>.

The spontaneous organicism was central in Menger's methodological work as well as in his article on the origin of money (1892), and became the core of the revised version of his *Principles*. It is worthy to keep in mind that Hayek maintained that Menger's aim was "to trace the complex phenomena of the social economy to their simplest elements which are still accessible to certain observation" (Hayek 1978, 276). Nevertheless, according to Hayek, by starting from these known elements it's possible to combine only certain stable structures: "Carl

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<sup>4</sup> At that time, Schäffle was very popular in Germany, and Menger read and quoted him in his works. The possible connection with biology and the constructive use of biological metaphor in Menger's thought (which he shared with German thinkers) seems sharply in contrast with the recent interpretation by Hodgson (2005), who argues that even if biological metaphor was not directly attacked by Menger, he indirectly criticized it to such an extent that its usage diminished in Germany.

<sup>5</sup> This theme was central in his *Untersuchungen* and it was presented in the chapter on the origin of money in the first edition of his *Principles*.

<sup>6</sup> Menger was an eager reader of read Spencer's *Principles of Sociology* (Spencer 1876-97). In Menger's library (held at the Hitotsubashi University, Tokyo) there exist many books by Spencer, including Spencer's *Encyclopedia of Social Facts* (in eight volumes, Spencer 1867-97), where Menger wrote copious notes and marginalia. Spencer's *Encyclopedia* is an enormous collection of data about language, markets, political organizations, etc., that he collected worldwide. Spencer used those data in order to write his *Principles of Sociology*. Menger's notes reveal he was mainly interested in understanding the origin of money and the nature of labor as well as trade.

Menger was quite aware of this limitation of the predictive power of the theory he developed and he felt that more could not be achieved in this field” (278)<sup>7</sup>.

## **2. On Social Needs and Goods**

The use of biology to describe the complexity of an economy allowed Menger to take into account not only individuals as economic agents, but also groups as economic agents: like individuals, social groups have their own needs (social needs). Social groups have a double nature: they can be regarded either as the sum of the individuals that form a group, or as something far more complex than merely a collection of individuals. According to Menger “societies, associations, corporations, communities, and the States” are complex social groups<sup>8</sup>: he defined them as “human associations” [p. 7]. Similar to other economic agents, human associations have their own needs (Bedürfnisse menschlicher Verbände) to be satisfied by proper economic goods (social goods). Social goods are the means to satisfy social needs.

According to Menger, there are three kinds of social goods: ‘common goods’, ‘collective goods’ and ‘goods of associations’. Common goods satisfy common needs: a common need of many individuals may be satisfied by each of them separately (the need for drinking water by separate house wells) or jointly by a single well (e.g., owned by a monopolist). Collective goods satisfy

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<sup>7</sup> Hayek wrote: “if we were to derive from our knowledge of individual behavior specific predictions about changes of the complex structures into which the individual actions combine, we should need full information about the conduct of every single individual who takes part” (277).

<sup>8</sup> The German equivalents are “Gesellschaften, Genossenschaften, Korporationen, Gemeinden, Staat, Volks- und Weltwirtschaft”.

collective needs: they arise when people who share the same common need (transport facilities or schools) require goods able to satisfy any individual need and a delegate agency is able to provide those goods demanded by the community as a whole. They correspond to the modern meaning of "collective" or "public goods". This social group is composed by the sum of all individuals who share the same common need. The third kind of social needs, the 'need of human associations', is a set of needs shared by individuals who are voluntarily linked in a particular association ('institution') and able to provide goods required by the members of that association in order to satisfy not an individual need commonly shared, but to satisfy a need of the human association as a whole.

As soon as institutions arise, they cease to be merely means to satisfy common needs: they acquire their own needs, and they are no longer the sum of single individuals but a whole that is more than the sum of its parts. Institutions become new economic agents with their own needs, which have the ability to influence individual choices.

This addition of a more complex economic agents (human associations) to individual agents, led Menger to shift from a pure individualistic approach to a more complex perspective: it's not the simple idea according to which social pressure and social rules can influence individuals' choices, rather it's the introduction of human association as a new economic agent. And this approach is quite similar to the German Historical school point of view. It should be noted at this point the fact that Menger's personal *querelle* against Schmoller did not cancel the deep influence that the old German Historical School (mainly Roscher) had on Menger (Yagi 1993, Ikeda 1995, Ikeda 2008)<sup>9</sup>. It was Hayek who had always tried to shade Menger's affinities with

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<sup>9</sup> There are many similarities in fact between Menger and (at least) the old German Historical School. The struggle between Menger and Schmoller was mainly a personal issue that faded away after few years.

German tradition, and who had insisted on Menger's similarities with Scottish tradition (Hayek 1934, 406)<sup>10</sup>.

The introduction of human associations should not be regarded as an eventual distance from individualism in the latest Menger text, rather as a development of his initially strict individualism toward a more complex approach. He was not interested in any ontological definition: he never claimed that the human associations can be considered as a sort of "Uber-economic-agent". Menger was interested in the causal connection amongst events: human needs are the cause of economic goods; and goods become economic when they are the effects of human needs in a context of scarcity. Human needs are individual as well as social, because along with individuals there are some particular social groups (human associations) whose nature is too complex to be considered just as a sum (of individuals). Human associations exist on complex levels of order magnitude higher than individuals that spontaneously emerge during human history.

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Also, the influence of Roscher was central in Menger's thinking, and this is not well recognized to any significant degree: historians seemed to consider Menger as a watershed in German speaking countries by highlighting the break between him and the German economists of the Historical School during the *Methodenstreit*. Unfortunately, the idea of a sharp division between Menger and the German School is still the dominant point of view among historians of economic thought. Reading the second edition of Menger's Principles, the "German influence" on Menger is even stronger above all if we think about the rise of institutions in the new first chapter (on human needs) where a kind of "holistic approach" to social goods seems to be present.

<sup>10</sup> Some authors had already underlined the presence of two methodological approaches in Menger's writings (Shearmur 1990); "in Menger's vision an 'organistic' approach to social phenomena in no way conflicts with an atomistic analysis in terms of exact economic theory" (Krabbe 1988, p58); as well as the differences between Menger's and Hayek's point of view on institutions: Menger's organic approach (compatible with what he called "the exact orientation of theoretical research") versus Hayek's subjectivism based on the central notion of cultural evolution and on the coordination of individual actions in a framework of dispersed knowledge (Garrouste 1994).

## **Conclusions: the meaning of entangled political economy in neo-Mengerianism**

A few relevant elements in Menger's *Principles* lead the reader to consider him as a possible forerunner of Wagner's entangled economy. The link between human needs and economic goods as a form of ecological approach to economics represents the most relevant aspect of the affinity between his late work and Wagner's entangled economy. Wagner himself, when presenting "neo-Mengerian" approach, starts from an inquiry into the relation between mind and society, and between society and environment.

The urgency of reconnecting economy and polity, that is fundamental in an entangled economy, is present in Menger. Wagner mainly refers to Menger 1883: when he recalls the distinction between the two "exact" address and "empirical-realistic", but instead of considering the former as the most important one (as it has always been done in order to emphasize the distance between Menger and German historicists), Wagner stressed the importance of the latter, that is related with any possible application between economy and its historical context. (Wagner 2010, XX). Entangled economy is as well implicitly present in the last Menger publication: because of the nature of human associations, any tentative consideration of economic activity as a set of rules separate from polity is incoherent, and, in a certain way, it is a naïve representation of economy that does not take an account of the complexity of social orders.

'Entangled, not separated', as Wagner writes about the nature of politics, markets, and political economy, when he invites economists to avoid the old fashioned contraposition between markets and states, economy and polity. States like markets are "polycentric networks of human relationships", they are not "organizations that exist apart". The four quotations from Menger at the beginning of this paper represent how he developed the idea that the State, market, and

money are not organizations: rather they are orders, or better said, networks, where agents spontaneously coordinate their choices and where there is no room for a sharp distinction between economy and polity.

In the first edition of his *Principles* (1871), Menger adopted a strict individualism: only individuals exist as economic agents. A decade later, in his methodological book (1883), Menger started to consider a national economy as an organism where economic laws (that exist) are applied in a context that has been developing in a more and more complex way. A decade later in his article on the origin of money (1892), the role of the State starts to be seen as necessary to fix and to adjust a social institution like money. In his last work (1923), that was composed after twenty years of studies and research in anthropology and sociology—as testified in his library—, Menger clearly considered ‘human associations’, including states as an economic agents: they have their own needs that require special economic goods (social goods). Human associations are not merely organized by individuals: they are spontaneous orders where economy and polity are connected in a natural and complex way. This final passage makes Menger a legitimate forerunner of Wagner’s entangled political economy and it paves the way to the neo-Mengerianism, i.e., a new reading of Menger’s thoughts as a whole.

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