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## Rejoinder to Brian Simpson's comment on Money, Banking and the Business Cycle

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The Austrian School's methodology underpins the Austrian Business Cycle Theory (ABCT). In his book and his reply to my review, Brian Simpson upholds the ABCT but rejects its methodology. That's nonsensical: non-Austrians have no counterpart to the ABCT precisely because their empirical approach and Austrians' praxeological methodology are chalk and cheese. In order to deduce the *Austrian* (as opposed to the Objectivist or other) business cycle theory, one *must* reason aprioristically. Simpson doesn't; hence I criticise him primarily because he draws his conclusions (which Austrians have deduced correctly) invalidly. In this rebuttal,<sup>178</sup> I do two things:

1. refute Simpson's criticism of the apriorism of the Austrian School. I show that the crux of his criticism - namely the assertion that "there is no knowledge independent of experience" - is false. Yet his criticism is an example of the human action he criticises; as such, it affirms Austrian methodology. Simpson, in short, scores an own-goal.

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<sup>178</sup> I thank the editor for the opportunity to provide this response to Brian Simpson's article which appears as 'Response to Chris Leithner's review of *Money, Banking and the Business Cycle*' (2014) 3 *Journal of Peace, Prosperity and Freedom*. My original review is in the same volume.

2. demonstrate that if Objectivists (Simpson identifies himself as one) took Ayn Rand at her word, then they too would be apriorists (albeit of a Rothbardian rather than a Misesian or Hoppean hue).

### EVER HEARD OF EFTPOS?

In my review, following the Austrian (particularly Hoppean and Rothbardian) approach in an encapsulated form, I show why money market deposit funds and travelers' cheques are not, as Simpson asserts, components of the money supply. Considered in isolation, this mistake (from a praxeological point of view) is hardly a major matter. What's cumulatively significant, however, is that a multitude of other errors mar Simpson's book. Given that I find the Austrian position compelling, and that his reply largely restates points or inferences in the book, it's hardly surprising that I found his reply unpersuasive. Rather than repeat what I've already said or respond point-for-point to Simpson's reply on this matter, I invite you to decide for yourself.<sup>179</sup> One point, however, I will make (and another I'll foreshadow).

Simpson challenges me to pay for groceries with funds from a cheque account without writing a cheque. He seems unaware that, through the use of Electronic Funds Transfer at Point of Sale (EFTPOS) technology, approximately 2-3 million Australians do precisely this every day. If you use EFTPOS at (say) a Coles supermarket, you instruct your financial institution to transfer the amount of your purchase from your cheque account directly to Coles's nominated account. According to the Australian Payments Clearing Association, in 2013 780,000 EFTPOS terminals across Australia, distributed among 325,000 individual businesses, processed more than 2.4 billion transactions whose combined value was approximately \$A135 billion.<sup>180</sup>

<sup>179</sup> For generalists, the most readable elaboration of the Austrian conception of money and its components – which my review followed and which, it seems to me, refutes Simpson's assertions comprehensively – is Michael Pollaro, 'Money-Supply Metrics, the Austrian Take' *Mises Daily*, 3 May 2010. More detailed and scholarly but still very readable treatments (which draw the same conclusion) include Murray Rothbard, 'Austrian Definitions of the Supply of Money' in Louis M. Spadaro (ed), *New Directions in Austrian Economics* (Sheed Andrews and McMeel, 1978) 143-156; Joseph Salerno, 'The True Money Supply: A Measure of the Supply of the Medium of Exchange in the US Economy' (Spring 1987) *Austrian Economics Newsletter*; Joseph Salerno, 'Ludwig von Mises' Monetary Theory in Light of Modern Monetary Thought' (March 1994) 8 *The Review of Austrian Economics* 71-115 and Frank Shostak, 'The Mystery of the Money Supply Definition' (Winter 2000) 3 *Quarterly Journal of Austrian Economics* 69-76.

<sup>180</sup> Lest Simpson retort that debit cards and EFTPOS are identical to cheques, notice that the writer of a cheque figuratively pushes on a rope: he cannot force money out of his account and into the recipient's account. Instead, the cheque-writer is effectively handing the far end of the rope

It's churlish of me to assume that Simpson possesses any knowledge of the electronic clearance system in Australia; charitably, one should assume that he's never set foot in Oz. On the other hand, in his reply he emphatically denied what in my review I mentioned as an aside: namely that the senses are fallible. My dictionary (an old *Canadian Oxford*) defines the word "fallible" as "(of persons) liable to err, especially in being deceived or mistaken." Everybody's senses are fallible in the sense that nobody can see (or smell, taste, know, etc.) everything. Yes, instruments ranging from the most primitive telescope to the most advanced electron microscope have improved (subject, it's important to add, to various assumptions which are themselves fallible) our senses. But nobody, it seems to me, can plausibly maintain that we can today or will someday be able to detect everything. Having accepted (and, I think, won) his challenge, could it possibly be that Simpson's – like everybody else's including mine – senses are fallible?

#### **THERE IS CERTAIN KNOWLEDGE INDEPENDENT OF EXPERIENCE**

In what I take as the crux of his reply to my review, Simpson asserts: "There is no knowledge independent of experience". If he had limited the scope of this assertion to an empirical science such as psychology, he'd be correct; but he applies it to an a priori science, namely praxeology (economics), and it's not difficult to demonstrate that he's mistaken. In short, economics is a body of knowledge; this knowledge (and knowledge of other important things too, such as causality) is independent of experience; hence knowledge independent of experience does exist.

What is the subject matter of economics, and what kind of propositions are statements about economic phenomena? Ludwig von Mises's (and Murray Rothbard's and Hans-Hermann Hoppe's) answer is that economics is a branch of praxeology – that is, the science of human action. What is human action? Mises couldn't be clearer:

Its statements and propositions are not derived from experience. They are, like those of logic and mathematics, a priori. They are not subject to verification and falsification on the ground of experience and facts. They are both logically and temporally antecedent to any comprehension of historical facts [or other "data"].<sup>181</sup>

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to the payee, who'll pull in his own good time. In this sense, EFTPOS is a contemporary version not of a cheque (which is a negotiable instrument) but of a wire transfer (which isn't): the payer pushes his money from his account into the recipient's – who cannot, unlike the endorsee of a cheque, repush it to a third party before it reaches his account.

181 Mises, *Human Action* (Regnery, 1966) 32.

This conception distinguishes the Austrian School – and specifically Misesians – from everybody else (including Simpson). Today, all non-Austrians regard economics not as a kind of applied logic but rather as an empirical science – that is, as a body of knowledge whose essence is the development of hypotheses whose verification requires extensive empirical testing (see, for example, page 4 of volume 1 of Simpson’s book). It’s vital to appreciate that this is a relatively recent development: until the Second World War, Mises’s apriorism was unremarkable. Quite the contrary – although others didn’t use the phrase “a priori,” Mises’s position was thoroughly orthodox. Leading mainstream economists such as Jean-Baptiste Say, Nassau Senior, John Cairnes, Frank Knight and Lionel Robbins, for example, conceived economics much as Mises did.<sup>182</sup>

How to substantiate the claim that praxeology – and thus economics – is a non-empirical science? As a preliminary example, consider this proposition: “Two people, A and B, undertake voluntary exchange only when both expect to benefit thereby. They expect to profit when A values what he receives from B more highly than what he trades to him, and B values what he receives from A more highly than what he trades to him.” How does one establish whether this proposition is true? Is the process of validation the same as that which occurs in empirical sciences? Does it require extensive trial and error, perhaps in order to find the range of circumstances in which it applies?

It’s quite obvious – except to virtually all of today’s academic economists, including Simpson – that the answer to these questions is clearly “no.” That A and B must expect to benefit, and that each possesses the reverse preference ordering vis-à-vis the other, follows logically from an everyday and common-sense understanding of exchange. Whatever the time, place, circumstances and parties to the exchange, it’s simply inconceivable that it has ever been, is now, or could ever be different. It is, in other words, incontestable that every purposeful, acting person always prefers what satisfies him more over what satisfies him less. It’s absurd to think that continuous empirical testing could somehow “establish” such a proposition. It’s equally silly to “establish” the theorem of Pythagoras by actually measuring the sides and lengths of triangles in Australia, Europe, in jungles and deserts, at the bottom of the ocean in a submarine, atop Mount Everest, etc. In Hoppe’s words, “[t]o think that either mathematical or praxeological propositions must be empirically tested is a sign of outright intellectual confusion.”<sup>183</sup>

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<sup>182</sup> For a full corroboration see Hoppe, *Economic Science and the Austrian Method* (Ludwig von Mises Institute, 2007) 10-14, from which this section draws heavily.

<sup>183</sup> Ibid 16.

But Mises doesn't merely notice this rather obvious and fundamental difference between economics and empirical sciences, he also clearly shows how and why a unique discipline like economics – which tells us about reality without requiring observations from reality – can possibly exist. Indeed, according to Hoppe this demonstration is perhaps Mises' supreme achievement. Following the Prussian philosopher Immanuel Kant (1724-1804), and particularly his major work, *Critique of Pure Reason* (1781), Mises classifies all propositions in a two-fold way: on the one hand they're either analytic or synthetic; and on the other they're either a priori or a posteriori. A proposition is analytic if formal logic is sufficient to ascertain whether it's true or false; otherwise, it's synthetic. A proposition is a posteriori whenever observations are necessary in order to corroborate it. If observations are not necessary in order to demonstrate its truth, then the proposition is a priori.

Kant upholds (and, as a Kantian, so does Mises) the existence of propositions that are simultaneously (1) a priori, (2) synthetic and (3) true. Unlike the truth of synthetic a posteriori propositions, the truth of synthetic a priori propositions can be established with certainty. In order to do so, the means of formal logic are necessary but not sufficient and observation is unnecessary. How does one establish the truth of such a proposition? The gist of Kant's answer is that it follows from self-evident axioms. What makes such axioms self-evident? One cannot deny their truth without self-contradiction; that is, any attempt to deny them necessarily concedes that they're true.

How do we find such axioms? By introspection, Kant says, and in particular by acknowledging the undeniable fact (Simpson, in his reply, rightfully demands that analysis be grounded in “the facts”) that we are conscious and purposeful, i.e., acting beings. This fact – as well as the fact that the truth of a priori synthetic propositions derives from introspection – also explains why such propositions can possibly possess the status of necessary truths. But Mises goes one step further: these truths are not simply categories of an individual's mind – but of his mind as an acting agent in the real world. Mises's conception of action bridges the gulf between the inner (mental) and exterior (physical) worlds. Misesian action, in other words, is simultaneously abstract thought and concrete reality.

Mises, then, solves Kant's problem – namely, how is it that true synthetic a priori propositions can exist? The axiom “humans act” (the verbose version is “humans act purposefully”) fulfils the two requirements for such a proposition. First, since the denial is itself an action, nobody – including Simpson – can possibly deny the existence of human action; hence the proposition is self-evidently true and cannot be challenged. Secondly, the axiom hasn't been derived from observation:

try as they might, neither Simpson nor anybody else can observe anything except bodily movements and sounds. Just as nobody can observe causality, they cannot observe purpose. Only by introspection can anybody recognise that certain movements, sounds, etc., are purposeful.

Clearly, then, human action is a category of knowledge that must be understood rather than observed; equally clearly, however, it's still knowledge about reality. It's not experiential, yet it's undeniable: through every action the actor pursues a goal; and whatever the goal may be, the fact (Simpson, remember, insists that we stick to the facts) that it's pursued by an actor reveals that the actor places a higher value upon it than any other goal that he could have conceived when he commenced the action. It's not empirical, yet it's real: in order to achieve his most highly valued goal, an actor must choose among competing and scarce means. It's not visible, but it's obvious: as a consequence of choosing means and preferring one goal rather than another – and of not being to realise all of his goals, at least not simultaneously – each and every action implies that the actor incurs costs. And lastly, it's not observable, but it's as plain as day: at the starting point of every action, the goal must be worth more to the actor than its cost, i.e., it must be capable of yielding a benefit whose value the actor ranks higher than those of the foregone opportunities (“opportunity costs”). Yet every action invariably faces the possibility that the actor finds, retrospectively, that the result actually achieved has – contrary to previous expectations – a lower value than the relinquished alternative might have had. Every action, in short, necessarily entails the possibility of profit and success – but also of failure and loss. As Hoppe (p. 24) puts it:

all of these categories – values, ends, means, choice, preference, cost, profit and loss and time and causality – are implied in the axiom of action. Yet, that one is able to interpret observations in such categories requires that one already know what it means to act. No one who is not an actor could ever understand them. They are not “given,” ready to be observed.

Mises's great insight – and the Austrian School's methodological basis – is that the foundation of true reasoning about economics lies in this conception of action; and the status of economics as a sort of applied logic, in turn, derives from the status of the axiom of human action as an a priori-true synthetic proposition. In *Human Action*, Mises derives the laws of exchange, the law of diminishing marginal utility, the Ricardian law of association and gains from trade, the law of price controls and the quantity theory of money – indeed, the entire corpus of Austrian School

economics including the ABCT – from this axiom. Rothbard does the same and ploughs new paddocks in *Man, Economy and State* and *Power and Market*.

#### WHY AREN'T RANDIANS APRIORISTS?

It's easy to anticipate Simpson's reply: "as an Objectivist, I'm an Aristotelian and not a Kantian; hence I (and other Objectivists) reject apriorism." Yet it's easy to show that if Objectivists took Ayn Rand at her word then they, too, would be apriorists! To understand why, let's establish some context. The twentieth century's most prominent Austrians – namely Mises, Friedrich Hayek and Rothbard – spoke sympathetically about Rand's free-market posture.<sup>184</sup> Rand didn't, by and large, return the favour. Quite the contrary: she denounced Hayek and Rothbard as "enemies" – Hayek because he compromised with statism and Rothbard because he greatly extended and elaborated anarcho-capitalism.<sup>185</sup> But Rand was much more positive – indeed, enthusiastic – about Mises: she vigorously promoted him and published enthusiastic reviews of several of his books including *Human Action*, *Omnipotent Government* and *The Anti-Capitalist Mentality*. She also applauded many of Mises' most distinctive ideas, such as the impossibility of economic calculation under socialism.<sup>186</sup> Indeed, Rand described her ideal curriculum as "Aristotle in philosophy [and] von Mises in economics ..."<sup>187</sup>

**184** According to Alan Ebenstein, *Friedrich Hayek: A Biography* (Palgrave, 2001) 275, although she didn't regard herself as an economist Hayek praised Rand as "one of three outstanding woman economists" (he didn't say who the other two were). According to Barbara Branden, Mises hailed Rand as "the most courageous woman in America" (*The Passion of Ayn Rand*, Doubleday, 1986, p. 189). Rothbard called *Atlas Shrugged* "the greatest novel ever written" (quoted in Justin Raimondo, *An Enemy of the State: The Life of Murray N. Rothbard*, Prometheus, 2000, p. 118). Later Rothbard became sharply critical of Rand, but more for her dictatorial manner, tyrannical ways and cult-like following – which included her demand that Rothbard abandon his beloved wife – than for her private-property, free-market and pro-capitalist stance, which he applauded (see in particular his "The Sociology of the Ayn Rand Cult," originally published in 1972 and republished in 2008 by LewRockwell.com).

**185** "As an example of our most pernicious enemy," Rand wrote in 1946, "I would name Hayek. That one is real poison" (see *The Letters of Ayn Rand*, ed., Michael S. Berliner, Plume, 1995, p. 308). And "I am profoundly opposed to today's so-called libertarian movement and to the theories of Dr Murray Rothbard," she hissed in 1974. "So-called libertarians," she rightly concluded – and I wholeheartedly agree! – "are my avowed enemies" (p. 664).

**186** See Michael S. Berliner (ed), *The Letters of Ayn Rand* (Plume, 1995) 515.

**187** Rand, *Philosophy: Who Needs It* (New American Library, 1985) 81. "Beginning in the late fifties and continuing for more than ten years," wrote Barbara Branden, *The Passion of Ayn Rand* (Doubleday, 1986) 188, "Ayn began a concerted campaign to have [Mises's] work read and appreciated: she published reviews, she cited him in articles and in public speeches [and] recommended him to admirers of her philosophy. A number of economists have said that it

Yet Rand's endorsement of *Human Action* was hardly unequivocal. Most notably, in the comments she scribbled in its margins<sup>188</sup> she condemned, among other things, Mises's aprioristic epistemology.<sup>189</sup> More generally, she averred that although "I do agree with many of its purely economic ideas," the Austrian School is "one of the many approaches to capitalism which I oppose".<sup>190</sup>

Roderick T. Long shows that Rand's disagreements with Mises were – like my disagreement with Simpson – mainly about broader philosophy and epistemology rather than the details of economics *per se*.<sup>191</sup> Why did Rand take the "gravest exception" to Mises's "general doctrine of praxeology"? "There is no 'a priori' knowledge," she insisted; "[t]here is no knowledge not derived from experience".<sup>192</sup>

Simpson's criticism of the Austrian School reflects Rand's. But if Rand and Simpson are correct, then how does a mathematician prove that  $1+1=2$ ? "By looking at two apples!" an Objectivist might reply. But a dog (much of whose sensory apparatus is superior to a human's which Simpson doesn't accept is fallible)<sup>193</sup> can also see the apples – and yet doesn't know arithmetic. How on earth can anybody possibly "experience" the fact that the sum of the lengths of any two sides of a triangle must be greater than or equal to the length of the remaining side? Or are Rand and Simpson seriously asserting that mathematics doesn't qualify as knowledge? In his reply to my review, Simpson states "an a priori belief in knowledge leads to ... the arbitrary. If one believes 'knowledge' is gained apart from observa-

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was largely as a result of Ayn's efforts that the work of Von Mises began to reach its potential audience."

**188** See *The Letters of Ayn Rand*, 105; 141.

**189** Nathaniel Branden recalls how, since Rand always seemed "friendly, respectful, and admiring" toward Mises, and indeed "almost girlish in the way she complimented him on his momentous achievements," he was surprised to discover, when perusing her copy of *Human Action*, that the margins were "filled with abusive comments." When Branden asked Rand if she really thought that Mises was a "bastard," she replied: "As a total person, no. ... But if I focus on that aspect of him where he goes irrational, yes ..." (*My Years with Ayn Rand*, Jossey-Bass, 1999, p. 116).

**190** *The Letters of Ayn Rand*, 642.

**191** Roderick Long, 'Praxeology: Who Needs It' (2006) 6 *The Journal of Ayn Rand Studies* 299-316.

**192** See Robert Mayhew (ed), *Ayn Rand's Marginalia: Her Critical Comments on the Writings of Over 20 Authors* (Second Renaissance, 1995) 113–14.

**193** Simpson makes this claim amidst an amusing – because it's so laughably inept – tirade against Holy Scripture. Simpson takes it as given that sense experience occurs in the eye (or nose or fingertips, etc.) But surely eyes and brain are each individually necessary and jointly sufficient conditions of sight? Without a brain to process the signals from the eyes, in other words, can anybody see? Second, for the sake of argument let's assume as Simpson insists, namely, that the senses are infallible. But if so, why isn't the brain? And if the brain, too, is infallible, aren't we all gods? But as an Objectivist Simpson stridently rejects the very possibility that there's a god – unless, of course, it's Ayn Rand!

tion, then anything goes". That's plainly silly: nobody who knows anything about mathematics could possibly assert that it's arbitrary. Similarly, nobody who's read Hoppe, Mises or Rothbard dispassionately can credibly allege that their premises, reasoning and conclusions are ad hoc.

Consider now Rand's proposition that capitalism is "a social system based on the recognition of individual rights, including property rights, in which all property is privately owned".<sup>194</sup> How did she justify it? Clearly, she couldn't possibly do so via any appeal to "the facts": for the undeniable fact – which Rand herself acknowledged – is that capitalism as Rand conceives it has never existed, that it's an unknown ideal, and what doesn't exist one simply cannot observe. If "there is no knowledge independent of experience" then on what basis can Rand, Simpson or anybody else conceive something that neither she nor he or anybody else has ever experienced? Long answers this question: "everything Rand says about 'capitalism' is thus an exercise in innocently a priori reasoning".<sup>195</sup>

To understand how Long reaches this conclusion, consider as well a form of reasoning that most philosophers would accept as a priori, which I utilised in my review, the previous section of this article and which Rand herself accepts – namely, the validation of axioms by demonstrating that the very attempt to deny them necessarily presupposes their truth. As Rand decreed,

there is a way to ascertain whether a given concept is axiomatic or not: one ascertains it by observing the fact that an axiomatic concept cannot be escaped, that it is implicit in all knowledge, that it has to be accepted and used even in the process of any attempt to deny it.<sup>196</sup>

As Long showed, Rand seemed – and, in his reply, Simpson seems – to be unaware that in this respect Rand conforms precisely to Mises. Rothbard restates Mises in a way that Objectivists cannot (unless they contradict Rand's quote above) reject:

The action axiom, in particular, should be, according to Aristotelian philosophy, unchallengeable and self-evident since the critic who attempts to refute it finds that he must use it in the process of alleged refutation. Thus, the axiom of the existence of human consciousness is demonstrated as

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**194** *Capitalism: The Unknown Ideal* (New American Library, 1986) 19.

**195** Long, 'Praxeology: Who Needs It' (2006) 6 *The Journal of Ayn Rand Studies* 308-309.

**196** Harry Binswanger and Leonard Peikoff (eds), *Introduction to Objectivist Epistemology* (Meridian, 1990) 59.

being self-evident by the fact that the very act of denying the existence of consciousness must itself be performed by a conscious being. ... A similar self-contradiction faces the man who attempts to refute the axiom of human action. For in doing so, he is ipso facto a person making a conscious choice of means in attempting to arrive at an adopted end: in this case the goal, or end, of trying to refute the axiom of action. He employs action in trying to refute the notion of action.<sup>197</sup>

Thus, given what Mises and Rothbard mean by “a priori,” Rand – and her acolytes like Simpson – should therefore be every bit as apriorist as Austrians!

Although they differ regarding the *precise epistemic status* of axioms, both Mises and Rand affirm their *general existence*. In principle, then, nothing prevents Rand and her followers from embracing the notion of human action and deducing therefrom – that is, from utilising the methodology of the Austrian School. Rothbard shows them how to embrace praxeology on exactly these grounds:

Ludwig von Mises, as an adherent of Kantian epistemology, asserted that the concept of action is a priori to all experience, because it is, like the law of cause and effect, part of “the essential and necessary character of the logical structure of the human mind”. Without delving too deeply into the murky waters of epistemology, I would deny, as an Aristotelian and neo-Thomist, any such alleged “laws of logical structure” that the human mind necessarily imposes on the chaotic structure of reality. Instead, I would call all such laws “laws of reality,” which the mind apprehends from investigating and collating the facts of the real world. My view is that the fundamental axiom and subsidiary axioms are derived from the experience of reality and are therefore in the broadest sense empirical.<sup>198</sup>

Rothbard calls such axioms a priori because, although they’re grounded in reality, they’re prior to “the complex historical events to which modern empiricism confines the concept of ‘experience’”.<sup>199</sup> This, given Rand’s pronouncement, is the sort of apriorism to which Simpson cannot reasonably object. Hence his – and Rand’s – objection to the apriorism of the Austrian School collapses.

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<sup>197</sup> Rothbard, ‘Praxeology: The Method of Austrian Economics’, *The Logic of Action I: Method, Money and the Austrian School* (Edward Elgar, 1997) 68.

<sup>198</sup> Ibid 63-64.

<sup>199</sup> Ibid 65; see also Rothbard, “In Defense of ‘Extreme Apriorism’”, *The Logic of Action*, 100-108.