

“Austrian” Subjectivism vs. Objectivism Part II

[first published in The Free Radical #56, May-June 2003]

In the first part on the topic, I showed that at least the early economists of the Austrian School of Economics based values on the same ultimate standard as Objectivism, i.e. life itself. I then proceeded to explain how the so-called subjective value theory of the “Austrians” could be reconciled with the objective value theory of Objectivism. This was made with the help of what I called contextual individual objective values (CIOV).

According to CIOV, values depend on contexts. And contexts are closely connected to the individual valuer, who’s life is the ultimate standard of those values.

CIOV vs. Objectivism

As I have already noted, I believe the concept of CIOV is fully consistent with the ideas of Ayn Rand. This involves the idea that the ultimate standard of value being the life of the valuer, the idea that values are contextual, the idea that the context is central to all value judgments and the idea that goods have no intrinsic value. Furthermore, I think it reinforces the fact that because man is not omniscient, his life depends on trying to study the facts and do the best he can to evaluate them. (This also has bearing on the impossibility of central planning. This is because with CIOV, the objective values a central planner has to try to find, now are extended to possibly every living person. This could help explain why the collectivist governments have gotten rid of so many persons - it simply facilitates planning! The more homogenous the persons are, the easier the planning is.)

But what about the idea that two individuals can reach different objective values of the same good? Well, if we start by recognizing that one and the same person can reach different valuations of the same good in different contexts, I think the rest follows. Otherwise, that would be a rejection of the theory of marginal utility, a thing Rand did not propound as far as I know. Instead, this reinforces the importance of clearly defining the context when one discusses different topics and passes value judgments. Moreover, it does not exclude the case where two individuals reach the same objective valuation, despite their obvious differences in income etc. For even if one individual for example has a different income from the other, they could nevertheless reach the same valuation. Furthermore, two persons can reach different conclusions even in a rather clearly defined context, without subjectivism being present. The differences in the contexts that stem from the special contexts of the individuals simply mean that the premises of the syllogism are different. And this does not exclude the possibility that one is right in saying to somebody that what they do is objectively not a good thing to do, it just suggests that one have to be a bit more careful in doing this to allow for possible objective differences in the persons lives.

With CIOV, I believe the importance and significance of each and every individual in the theory of value is manifested. There can be no value without a valuer, and the valuer is always an individual, and the standard of value applied to the concrete context of the valuer is the individual valuer's own life. This clearly is fully consistent with the ideas of individuality of Objectivism and the ideas present in the principles of natural rights.

CIOV vs. the Theory of Marginal Utility

I have mentioned the theory of marginal utility a number of times so far. I have not told the reader exactly what it says yet (most reader probably know it already). In 1871, Leon Walras, Stanley Jevons and Carl Menger independently published ideas leading to the theory of marginal utility. The theory was a revolution, since for the first time, the so-called value paradox of the classical economists could be solved. The value paradox consist of the fact that things that are not very useful for the life of human beings, like diamonds, normally could be more valuable than thing that are essential to the preservation of life itself, like water. The theory of marginal utility tells us that this is no paradox and this can be explained by the famous example made by Eugen von Böhm-Bawerk (*Capital and Interest*, Vol. 2, Book III, Ch. III, p.143-145). A short version of it is that we imagine a pioneer farmer who has just harvested five sacks of grain. The first sack keeps him alive, the second healthy, the third is used to feed the poultry, the fourth to distill brandy and the fifth to feed the parrots. Now, to use Böhm-Bawerk's own words, "what is the significance for his well-being of one sack of grain?" The answer is that any sack of grain is valued as the last, or marginal, sack. This follows since if our pioneer would lose the sack that is supposed to preserve his life, he would simply eat out of the fifth sack. It is feeding the parrots he would choose to forego if he lost a sack, not dying. From this the law of diminishing marginal utility follows, summarized as "The law of diminishing marginal utility states that the utility or, equivalently, the importance or personal value that an individual attaches to a unit of any good diminishes as the quantity of the good in his possession increases." (See George Reisman's *Capitalism*, p.49).

Hence, the law of diminishing marginal utility provides a perfectly natural explanation to the alleged value paradox. The water, that is necessary for life preservation, is less valuable than diamonds, that certainly not is needed for the mere preservation of life, simply because if someone lost a cup of water it could easily be replaced, while the same does not hold for diamonds. This law has to be applied to a specific context of the valuing individual. It is also perfectly natural if, in an extreme situation of a desert, an individual would value a cup of water higher than all the diamonds in the world, if obtaining the cup of water is the difference between life and death. Thus, Walras, Jevons and Menger provided a solution to the value paradox.

Now, is this theory consistent with CIOV? Yes, I believe so. The only thing that has to be realized is that the context of the pioneer farmer changes as he gains or loses one sack of grain. In the context of only having one sack, the value of the sack is the same as his life, and in the context of having five sacks, the value is the same as the last sack he uses to feed the parrots. As a proof of the idea that it is the context that determines the value, I believe it is extremely important to realize that it is the idea of differences in values between contexts that has to have been the idea that helped Menger to develop the theory of marginal utility, and not that values differ between individuals per se. The latter is just an effect of the former (regardless of the fact

that the existence of a valuer is a prerequisite of the value at all). Menger simply could not have developed the idea on basis of values differing between individuals per se.

Böhm-Bawerk provides us with what probably is the most developed version of the theory of marginal utility. This includes the analysis of capital goods, i.e. goods that are used in production of other goods. Although his view of value is not fully consistent with CIOV, the essence of his theory is not affected. One only has to keep in mind that he uses subjective and objective in a different way. One famous result of his is the fact that prices are determined by the marginal utility, but that this very often turns out to coincide with the case that prices are determined by cost of production. But the cost of production is in turn determined by the marginal utility of the factors of production. A crucial part of the explanation lies in that the many producers sees the many uses of a factor of production, and values them according to the marginal use of it. But how can many producers reach the same conclusion about the marginal use and value of the factor of production, if values are subjective? CIOV helps explain that they are objective, but the value of the factor of production depends on the context of the marginal use of it. So, also this part of his exposition of the theory of marginal utility fits in fine with CIOV. And this implies that Böhm-Bawerk really was on the same track as Menger. Moreover, we also see that the words by Mises quoted above - "they differ with various people and with the same people at various moments in their lives" - is consistent with the idea that values differ between contexts and hence between individuals. Thus, CIOV and the theory of marginal utility provide support for each other. They are fully consistent and one only has to make some almost semantic changes in the latter.

In connection to this I'd also like to comment on the following words by Mises (Human Action, p.28):

"Praxeology and history do not pretend to know anything about the intentions of an absolute and objective mind, about an objective meaning inherent in the course of events and of historical evolution, and about the plans which God or Nature or Weltgeist or Manifest Destiny is trying to realize in directing the universe and human affairs. They have nothing in common with what is called philosophy of history. They do not, like the works of Hegel, Comte, Marx, and a host of other writers, claim to reveal information about the true, objective, and absolute meaning of life and history."

These lines reveal that Mises thought that objectivity has something to do with mysticism or paternalism, as opposed to reality, implying that Hegel, Comte and Marx were objective. I believe this is implied also when he somewhat earlier in the book, (p.14) declared that:

"The ultimate goal of human action is always the satisfaction of the acting man's desire. There is no standard of greater or lesser satisfaction other than individual judgments of value, different for various people and for the same people at various times. What makes a man feel uneasy and less uneasy is established by him from the standard of his own will and judgment, from his personal and subjective valuation. Nobody is in a position to decree what should make a fellow man happier."

No wonder Mises escaped to subjectivism if he thought objectivity leads to socialism! He must have believed he had no other place to go. But what is it Mises really object to? Is it really objectivity? No, I believe it is the idea that economic goods have universal values, i.e. the same

value over all contexts, as for example in Marx' labor value theory. And then he continues by saying that they instead depend on the individual valuer. But since he supports the theory of marginal utility, he must really have supported that values depend on context, and only as a consequence of that, on the individual valuer. Hence, we see that the views of Mises are not really that far from CIOV or Objectivism.

There are at least two other aspects of economics that are related to values that Menger's theory does not answer that I would like to make some short comments on.

Are economic goods always valuable?

Remember Menger sorted out non-economic goods from the economizing activity of individuals. Non-economic goods were those that were available in quantities greater than our requirements. Instead individuals were economizing over goods that were available in a less quantity than our requirements. If an economic good ever became super-abundant, i.e. the requirements became less than the availability, it turned into a non-economic good, and vice versa. Menger tells us that non-economic goods cannot possess value. Does that mean that economic goods always possess value? Consider the following example: I have a limitless need for fast transportation. I need and desire a Porsche. I have a limitless need for food and drinks. I need and desire a soda.

In both of these cases the availability clearly is less than our requirements, i.e. the quantities of goods that an individual must have to satisfy his needs. These are classified as economic goods according to Menger. But do they necessarily possess value? This is a question Menger does not deal with, at least as far as I am aware. The theory of marginal utility does not provide an answer to this.

However, I think CIOV can provide a plausible answer to this: an economic good does not by necessity possess a value. This can be grasped by considering that a good can only possess a value to a valuer, in the context the individual is in at the moment of the valuation. When I say that a Porsche is valuable, and even more valuable than a soda, I am simply referring to the fact that a Porsche could be immensely valuable to me, if I ever were in the position to afford it. The statement refers to another context than the actual context of my life (as a Ph.D. student). Once this is grasped, it comes as no surprise that I end up spending \$1 for a soda and zero for a Porsche, since in the context of my life, the soda is worth \$1 and the Porsche not a thing. This helps explain why I do not put a value on all the wonderful and life-affirming things that are around. The Porsche may have a huge potential value, as opposed to the modest actual value of the soda. This is implied by the example of the table auction discussed in the first part. As we economize between economic goods, some just come out of question.

The statement that the Porsche is more valuable than a soda is fully in line with the fact that our needs and desires for wealth are limitless, only bounded by our imagination, but that our possibilities of satisfying them are limited. Most of our needs lie dormant until they come within the reach of ours. Ours what? Our capacity to gain access to the goods in question. In a modern monetary economy, our capacity to gain access to the goods in question is manifested as a budget restriction. Menger notes this when he writes about the relation between our requirements vs. the availability of goods. Thus, we have a limitless need for wealth but are restricted by our budgets. With the help of CIOV we actually can explain how scarce economic

goods can have no value to us. In a given context of an individual valuer, a good may be needed and desired, and at the same time scarce, but nevertheless possess no objective value to the individual. But as the context of an individual valuer is the only valid context, does this hold universally, economy-wide? No, because then I believe Say's law sets in, i.e. the idea of the classical economists that the production creates demand. If we are able to produce something as useful as a Porsche and actually already have produced it, then the demand would adjust so that to allow for this useful thing. In an exchange economy, the exchange rates between goods would adjust and in a monetary economy, the prices of goods would adjust so that the Porsche is afforded within the total circulation. Thus, the implication only holds with regard to the individual valuer, and not economy-wide. The implication of CIOV that economic goods need not possess value is new as far as I know. Perhaps the reader knows better. A further implication is that value-less things can include all of Menger's following categories: non-useful things, useful things, non-economic goods and economic goods. That is: every conceivable kind of thing in the material world!

This is easier to understand as one recollects that any particular object can move between the categories, but it is only as economic goods they can possess a value.

Stated value ex ante vs. CIOV

The second major example I can come up with that Menger's theory does not answer is the following: let us say I want to buy a new laptop. I say to my fiancée that I now can afford it since I have saved the money I think it will cost me. Assume this amount is \$1000. Then I head for the mall, only there I find that I only have to pay \$700. What is the objective value of the laptop? Well, it could easily be argued that it would be foolish of me to pay \$1000 for it, i.e. that would be a case of subjectivism. I will surely not pay more than the \$700. I argue that according to the idea of CIOV, the objective value is \$700. My ex ante valuation of \$1000 was in a context other than the actual context of the purchase. The difference between my ex ante valuation of \$1000 and the \$700 I paid was due to my misreading of reality (the context). Later I gained further knowledge about the facts of reality and learned that I could actually get it for \$700 and that that saved me some money for the satisfaction of some other need of mine.

The difference between what I say I am willing to pay and what I actually pay is called the consumer surplus in mainstream economics. This is something that is supposed to be maximized. If that is so, in the example of laptop, that means that what is supposed to be maximized actually is the difference that occurred due to my misreading of the real world context. What is maximized is ignorance. How strange can things be in mainstream economics?

I think most businessmen and persons into marketing would see the obvious difference between asking people what they want to pay for a thing, and what they find people actually later are paying. Recognition of this is actually a thing that sorts out good businessmen from bad. But observe, when businessmen try to figure out what people want, they do not try to figure out what people's subjective valuations are. That would be like rolling the dice, a thing a successful businessman would not let his success depend upon. And they do not try to find a thing of universal value, a thing that is as valuable in all possible contexts, because they know such a thing does not really exist. Instead, they try to figure out the needs and desires of people in the contexts of their lives. They try to find the objective value in a specific context, assured that if

they find it, others will to and they will become rich. That is the main objective of consumer segmentation etc in marketing. But in the global mass-markets of capitalism, one might also earn a fortune by selling goods to people who share subjective values, even things that could not be justified on rational grounds, provided there are a sufficient amount of people and purchasing power for it. Furthermore, in reality, where there often is no point in putting more effort into finding the exact objective value, the fine-tuning around an objective value takes the form of tastes. If I buy a white or a black car might be of minor importance objectively, unless I'm an undertaker, and my choice may fit into an overall pattern that is my taste of color. Hence, subjectivity might play an important role as well.

The idea of ex ante valuations vs. CIOV has the rather strong implication; the rejection of the theoretical difference between use value and exchange value. Remember that Böhm-Bawerk wrote that "Objective exchange value [i.e. Menger's exchange value] is one of the important results which it behooves economics to explain; subjective values [i.e. Menger's use values] belongs to the means or tools by which economics is to achieve some of its explanations." Could CIOV be the explanation? Use value being the ex ante estimate of the value and the exchange value the actual objective value within the context of the purchase.

The discussion in this section is to be seen as some first thoughts around the concept of CIOV. It provides some loose ends to study further. However, it implies some possibly fresh ideas, i.e. that (i) economic goods do not by necessity possess value, and, (ii) that there is no distinction between objective use value and objective exchange value. Any differences are due to subjectivity in the form of real life uncertainties and lack of time, i.e. to the fact that Man is not omniscient.

Final Comments

Does the concept of contextual individual objective values pave way for subjectivism by proposing that people can say that their valuation is valid to them, to their life? It is possible. It is a risk. But that only tells us to be even more careful in defining matters. The true subjectivism around us is certainly common and has a strong hold on many sciences. I hope the reconciliation of the wonderful ideas of both the Austrian School of Economics and the Objectivism of Ayn Rand as presented here will strengthen the case for objective meaningful values in life. I hope this presentation has showed that the ideas on value of Ayn Rand are in no essential way different than the ideas on value that Carl Menger, Eugen von Böhm-Bawerk and even Ludwig von Mises held.

And I hope the two great bodies of thought thereby could unite in the struggle for freedom and laissez-faire. Premises checked. Peace and love to you all.

Endnotes

i Menger's exposition was in his Principles of Economics. The term was coined by Wieser (1884), in German, i.e. Grenznutzen. See Friedrich von Wieser (1884), *Über den Ursprung und die Hauptgesetze des wirtschaftlichen Wertes*.