



How Compatible are Public Choice and Austrian Political Economy?

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Abstract. Public Choice relies heavily on equilibrium analysis in its models of government failure. Austrians are suspicious of equilibrium analysis owing to its reliance on some variant of the perfect-knowledge assumption. To what extent then can Austrians consistently embrace public-choice descriptions of government failure? This paper argues that to maintain methodological consistency Public Choice should jettison the equilibrium, perfect-information framework, while keeping the empirically relevant assumption of narrow political interest.

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“Policy failure has often been attributed to mistakes and ignorance, but it might rather be the result of the rational pursuit of interest and not really a failure from the perspective of those whose interests are controlling the choice at hand.”

Richard Wagner (1989:56)

“Economics does not say that isolated government interference with the prices of only one commodity or a few commodities is unfair, bad, or unfeasible. It says that such interference produces results contrary to its purpose, that it makes conditions worse, not better, *from the viewpoint of the government and those backing its interference.*”

Ludwig von Mises (1966:764, emphasis original)

At least since the appearance of Buchanan and Tullock’s *Calculus of Consent*, it is fair to say that practitioners of Austrian economics and Public Choice have generally felt a fairly strong sense of kinship. This has been so especially in terms of method—i.e., the use of the rational-choice approach (broadly construed) to study the political process—and ideology, in the form of skepticism toward political solutions to perceived social problems.¹ (This is perhaps truer of adherents of “Virginia” Public Choice.²) For example, the *Elgar Companion to Austrian Economics* contains an entry on public-choice economics, thus explicitly acknowledging the latter’s place within the Austrian research program. Despite broad areas of agreement, however, political economists working in the Austrian tradition ought to feel rather more equivocally toward certain aspects of Public Choice than they currently do.³

The reason for this ambiguity can perhaps be best understood in light of the Austrian critique of the neoclassical concept of market failure. That is, Austrian economists object to the

concept of market failure, not because it questions the feasibility of laissez-faire capitalism, but because of how neoclassical economics defines “failure.” Specifically, Austrians are unwilling to label a “failure,” in the manner of standard theory, any departure of a system, in practice or in theory, from some equilibrium-based benchmark such as Pareto optimality. They resist because current models of market failure, even those that have emerged more recently from neoclassical information theory,⁴ do not address what Austrians see as an essential aspect of the real social world—namely, radical ignorance and genuine error.⁵ The present paper is not a critique of the concept of market failure, however. Others have capably undertaken such criticisms elsewhere (Cowen 1992). It is in a spirit similar to those earlier criticisms, however, that it examines the Public-Choice approach to *government* failure.

There are actually two aspects to the Austrian critique of the very notion of failure in neoclassical economics. The first is that since, from the Austrian perspective, error is pervasive in the *real* social world, we would be committing the so-called Nirvana fallacy were we to use an unachievable, and indeed excessively unrealistic standard (i.e., general competitive equilibrium or global Pareto optimality), against which to evaluate it. The more correct approach, as Demsetz (1969) has effectively argued, is to compare the status quo with what it might have been under different but attainable conditions.

The second and, for this paper, more pertinent criticism stems from the fact that, in making the theoretical case against laissez-faire, neoclassical economics, even its more technically sophisticated varieties, asserts that departures of a system from Pareto-optimal equilibrium is ultimately the result of *information costs*. Now, adding significant information costs into a model naturally changes its equilibrium solution. If we were to ignore these added information costs, then the new equilibrium would naturally appear to be suboptimal when compared to the old equilibrium. But this simply means that when these information costs *are* taken properly into account the new equilibrium will be revealed to be genuinely optimal, while the old equilibrium will rightly appear to be suboptimal in the presence of these added costs. Thus, equilibrium theories of monopoly power, externality, and public goods, because of their essentially static nature, fail to explain why dynamic market forces would systematically overlook the profit opportunities implicit in each of these phenomena.⁶ Consequently, they are also silent on the question of how government intervention could cope better with these deviations than market forces when knowledge is less-than-perfect. Similarly, theorems such as Greenwald-Stiglitz (1986, 1988) that challenge the information efficiency of nearly every market in a capitalist system do not tell us how, without the protection of high transaction costs, asymmetric information would be able to persist, or why it is more reasonable to assume that the discovery of arbitrage opportunities should be costly rather than costless, as it is in Israel Kirzner’s Austrian concept of entrepreneurship (Kirzner 1973).⁷ A consistent neoclassical rendering of these kinds of situations should regard any deviation from an initial optimum, when it is the result of adding new opportunity costs, as itself optimal (i.e., there is an optimal degree of “suboptimality”).⁸

Still, the belief that Austrians are skeptical of market-failure arguments mainly for ideological reasons may be reinforced to the degree that Austrians uncritically embrace the neoclassically inspired theories of “government failure” that public-choice scholars have produced.⁹ For example, the public-choice theories of rational voter ignorance, rent seeking, and bureaucratic growth are essentially an application of the standard neoclassical

utility-maximization calculus to nontraditional equilibrium models in which nevertheless all relevant tastes, resources, and technologies (or their fully specified probabilities) are assumed to be known to the agents in the model. From the standpoint of positive economics, equilibrium models of politics, like equilibrium models of markets, may help to explain important aspects of real-world behavior. But also like their market counterparts, equilibrium models of politics tend not to theorize too deeply about what is arguably an intervention's most serious consequences—namely, those that are either unintended or unforeseen. Reasons for this lapse are presented here.

The main argument of this paper then is that an Austrian political economy that rests on an appreciation of the significance of radical ignorance (to be defined shortly) is better placed to explain the existence, and to trace the long-term repercussions, of the *unintended* consequences resulting from public policy. It also contends that Public Choice and Austrian political economy, in addition to their important differences in equilibrium orientation at the level of pure theory, also tend to view public policy from two dramatically different perspectives, but that these perspectives are complementary rather than competing. Indeed, it is upon this complementarity that the Austrian sympathy for Public Choice should be, and largely is, based (rather than on ideological sympathy) and, despite the fact that each of these perspectives follows directly from its particular attitude toward equilibrium, upon which a more unified theory of public-policy failure might be erected.

Tales of Deception and Error

Public Choice and what I have elsewhere (Ikeda 1997) termed “Austrian political economy” appear to adopt distinctly different starting points or facts-to-be-explained in their analyses. For Public Choice it is *the divergence between announced and actual intentions*. For example, a teachers’ union will claim that professional certification is essential to guarantee minimum levels of classroom competence, although it “really” favors certification as a means to lessen competition and raise teachers’ salaries. Or, bureaucrats will argue before Congress that significant increases in their annual budget is in the public interest, when all they “really” want to do is to maximize their turf and future political influence. Thus, a combination of high transaction costs (e.g., the cost of measuring the marginal productivity of teachers) along with asymmetric information (e.g., the fact that bureaucrats know more about their needs than Congress does) that enables opportunism to generate a divergence between announced and actual intentions, or what I will term for convenience “deception.” This term is appropriate since presumably if an intervention were intended to benefit the general welfare rather than some narrow self-interest, a majority of the public would tend to support it so that no political deception would be necessary in a democratic setting.

By contrast, the point of departure for Austrian political economy is *the divergence between intended and actual outcomes*, or what I will call “error.” In Ludwig von Mises’s classic analysis of price controls, for example, public-spirited regulators intend to simultaneously lower the price of milk and increase its supply by imposing a price ceiling, yet the actual outcome is the perceived need to regulate the prices of inputs used in milk production when an inevitable milk shortage develops (Mises 1977:15–55). The policy creates the unintended consequences of, initially, a milk shortage and then, secondarily, further regulation.

Ultimately there emerges a dynamic spiral of intervention that seems to take on a life of its own as it encompasses more and more markets. And because these negative consequences were unintended, it is plausible (though not necessary) to assume that the supporters of the intervention are well-intentioned, i.e., acting to promote the general welfare.

Arguably, each of these perspectives is the logical consequence of the methodological attitude that Public Choice or Austrian political economy takes toward equilibrium analysis. To see why, let us first note that one of the central ideas that define neoclassical economics is that of *perfect knowledge*, which refers to that state of affairs in which actors possess information relating to their future plans sufficient to avoid ex post regret. Where there is perfect knowledge, it follows that the future outcomes of present actions will never generate disappointment, i.e., what we expect to happen, and only what we expect to happen, will indeed happen. This identity of intended and actual outcomes means that there is no real possibility of error on the part of the actor. Faced with all relevant costs, benefits, and probabilities he will always make the right choice. But if actors always get what they want, in a world of perfect information it would seem to follow that they must have wanted what they have gotten. That is, the assumption of perfect information would also clear the way for the political economist to infer the actual intentions of public choosers from the outcomes of public policy. Indeed, Wagner advances straightforwardly from this position to argue that “Public choice theory is a proposition about inferring intentions from outcomes...” (1989:46–47). In the context of politics, this means that if we observe higher unemployment rates among marginally skilled workers as a result of a labor-union-supported increase in the minimum wage, we can infer that that is what those unions really intended. Once again, inferring intentions from outcomes under the assumption of perfect information (or perfect probabilistic information) implies that public choosers always get what they want, and what comes to pass is what they wanted to come to pass even if others suffer net harm by it as a result. *In a neoclassical framework, government failure does not mean that public choosers fail to produce the intended outcome with their policies, but that the intervention produces deadweight losses, which those public choosers are prepared to live with and no one else has an incentive to remove. In neoclassical fashion, therefore, the departure from Pareto optimality that a policy produces is a measure of policy failure.*¹⁰

In addition, Public Choice typically assumes that what motivates public choosers to support any given intervention is the desire to use relatively cheap political power to transfer private income or wealth from others to themselves (which makes it necessary to use deception). This means Public Choice treats deception, the divergence between announced and intended intentions, as an instrument that promotes narrow private interests over broader public ones.

It would of course be naive to believe that the use of deception to promote narrow political interests is not fairly common practice in the political process. Businesses and labor unions alike do press for protection from competition while using the rhetoric of public interest or social justice. For many it is almost reflexive these days to suspect that the politician who wears his heart *on* his sleeve must also have something hidden *up* it. But, on the other hand, to argue that one can always infer intentions from outcomes has some rather unrealistic implications of its own. Do those who support the legal prohibition of certain drugs really intend to promote drug addiction, violent crime, and educational decline?¹¹

Are raging inflation, chronic involuntary unemployment, and the business cycle really the outcomes that monetary authorities always desire? Hopefully, most (but apparently not all¹²) public-choice economists would deny that such is the case. The point is, however, that given the aim of inferring intentions from outcomes, it is not obvious on what methodological grounds they would do so. Here as elsewhere, an equilibrium-based paradigm such as Public Choice encounters a fundamental problem in dealing with phenomena that are generated by nonequilibrium forces. In any case, Public Choice has not for the most part pursued this line of inquiry as far as it has that of the intended outcomes of public policy.

Alternatively, one may view these phenomena as the unintended and frequently unwanted consequences of policy interventions. But a framework in which such unintended consequences could arise must, as the previous discussion suggests, jettison the assumption of perfect knowledge and with it the exclusive concentration on equilibrium analysis. In its place would be substituted the concept of partial *radical ignorance*. The adjective “radical” is here meant to distinguish this kind of ignorance from the neoclassical concept of rational ignorance, which refers to a state of affairs in which knowledge exists that would improve our situation but that the expected cost of acquiring it exceeds the expected benefit. We thus choose not to know what is not in our interests to know. In contrast, radical ignorance refers to our unawareness of even the existence of relevant knowledge that we could know at zero cost. It is the absence of perfect knowledge, in any of its various guises. In the presence of radical ignorance, actions may, indeed they undoubtedly always will to some degree, produce unintended consequences, desirable and undesirable, from the perspective of the actor.¹³ Thus, the dynamic linkages that connect anti-drug policy (which makes illegal drug trafficking lucrative) and long-term government-intervention into primary and secondary education (which seems to have made a large amount of investment in human capital a losing proposition) result, through ideological pressure and entrepreneurial political opportunism, in the failure of many urban public schools to adequately teach their students, and now to proposals for further government intervention in the form of national educational testing and uniform educational standards. The Austrian concept of government failure is thus very different from that of Public Choice insofar as the latter views government failure in terms of deviations from an ideal optimal state. *Government failure from the Austrian perspective refers therefore to the failure of an intervention to produce the outcome sought by its proponents.*¹⁴

Note that there is nothing in this approach that implies that public choosers are acting either in the public interest or in their narrow private interests. The tactic that Mises and other Austrians have generally, but not universally, employed, has been to assume, again contrary to Public Choice, that public choosers are “men and women of goodwill” who act to promote the general welfare or at least to do good for persons other than themselves. Mises’s milk-price-support story is a good illustration. This is in line with the Austrian method just explained of defining government failure from the viewpoint of an intervention’s proponents. Once again, however, the error approach does not entail such an assumption. Indeed, as we will see, this is the basis on which I argue in the conclusion that Public Choice and Austrian political economy might be combined to form some kind of unified theory of interventionism.

Finally, the Austrian method of political economy leads naturally to seeing different interventions being linked together over time. That is, the Austrian framework that views government failure in terms of “frustrated outcomes”¹⁵ would not only analyze or evaluate the impact of a given intervention on a set of initial conditions (which would include existing interventions and policies, relative prices, and ideological preferences), but it would also approach such tasks with an understanding, implicit in the very notion of government failure, that any given intervention must be seen as part of an on-going *process* with its own internal dynamic. Such a dynamic, the result of the interactions among only partially informed plans originating from within imperfectly coordinated governmental and catallactic processes, would drive the mixed economy either from one partly or wholly failed policy to the next or from one attempt at decontrol or “disintervention” to the next. The Austrian framework examines the specific character of that dynamic as it is manifested in different kinds of intervention (e.g., price versus nonprice regulation, regulation versus transfers).

Before doing so, however, it may help to distinguish the two methods defined thus far by presenting a schematic that I have used elsewhere (Ikeda 1997).

Here I have distinguished between two kinds of motive and knowledge assumptions. With regard to motive, public choosers may be either narrowly self-interested or benevolent. With regard to knowledge, one may assume that they either possess perfect knowledge or suffer from at least partial (radical or rational) ignorance. Using Rowley’s (1994) characterizations, Chicago Public Choice belongs in the upper-left quadrant (at the intersection of narrow interest and perfect knowledge), while Austrian political economy belongs in the lower-right quadrant (at the intersection of benevolence and partial ignorance). The reader should bear in mind that these characterizations pertain to what I regard as the essential and unique features of each approach, as I have tried to indicate in the Figure 1. Reality might actually lie somewhere in the “middle,”¹⁶ as many if not most imperfectly informed interventions appear to be plainly self-interested. Indeed, Mises and Hayek have in their writings often relaxed the assumption that “men and women of goodwill” hold the reigns of political power. In an analogous way, public-choice theorists, for example, Buchanan, Wagner and (early) Tullock, have departed from the assumption of strictly perfect information to examine the

		Motive	
		Narrow Interest	Benevolence
Knowledge Assumption	Perfect Knowledge	(UNIQUE) CHICAGO PUBLIC CHOICE	PUBLIC INTEREST VIEW
	Partial Ignorance	(UNIQUE) VIRGINIA PUBLIC CHOICE	(UNIQUE) AUSTRIAN POLITICAL ECONOMY

Figure 1. Knowledge-motive matrix of politico-economic systems.

implications of (rational) ignorance on the political process. Their work comes under the heading of Virginia Public Choice. Hence, it would be appropriate to place them, along with some of the statements of Mises and Hayek, in the lower-left quadrant. In general, however, as reflected in the statement from Wagner quoted at the beginning of the present paper, the bulk of what one might generally term Public Choice properly belongs in the upper-left quadrant, if in Austrian fashion we understand the concept of perfect knowledge to include rational ignorance.¹⁷

Nothing that I have said thus far, however, should be taken to deny that many adherents of Public Choice would find much of the theory and implications of government failure in the Austrian sense congenial to their own outlook. The point is that the *analytical* core of both Virginia and Chicago Public Choice consists of equilibrium models of behavior; and in the tension between models and rhetoric in Public Choice, as in most research programs, methodologically speaking it is the model not the rhetoric that will ultimately drive or constrain analysis. This is in evidence in the important place Public Choice gives to what I have called deception.

But note that while an equilibrium approach implies an emphasis on deception and narrow political interest, the latter as an analytical starting point does not necessarily entail an equilibrium approach. This is a theme that I will revisit at the conclusion of this paper.

Implications for Policy Analysis and Evaluation

This section attempts to outline some significant differences between these frameworks in the analysis and evaluation of public policy in several broad areas. The contention is that Austrian political economy extends in important ways any economic analysis of public policy that is based on standard microeconomic theory, including Public Choice. While these differences are indeed very important, my intent is not to suggest that practitioners of Public Choice necessarily would disagree with these extensions or even that they would find them particularly novel. Indeed, they themselves from time to time have at least to some degree undoubtedly used the process approach that I have identified here as characteristically Austrian.¹⁸ The issue is that their doing so is inconsistent from a methodological point of view unless they explicitly adopt a nonequilibrium perspective. Otherwise, such an inconsistency is likely to breed a level of confusion that can hinder the effective development of a sensible, unified framework of political economy.

Price Regulation in an Industry

We have already seen that with respect to price controls, Mises's analysis differs from that of standard theory mainly in the way it traces the longer-term disequilibrating effects and unanticipated outcomes of such controls. Standard analysis tends to focus primarily on the equilibrium deadweight losses that occur as output falls and the marginal willingness to pay rises above the marginal cost of production. Recall that Mises in his example of price regulation discussed not only the resulting shortages, but also the impact that the perception of these shortages will have on the incentive to intervene further of well-meaning, but only partially informed and ideologically driven. Essentially, what Mises describes is

an intertemporal “slippery slope” or “vicious cycle,” in which each intervention—into a dynamic market process in which at every moment actors are attempting to adjust to circumstances that they only imperfectly understand—is followed inevitably by unintended problems. These in turn, under prevailing ideological beliefs, incite further interventions and consequent problems, and so on.

Two points need to be made here. The first is that ideology plays a crucial role, for it is the regulators’ *belief* in the workability of interventionism that prompts them to respond to the shortage, not by removing the price control, but with further intervention (in the input markets). Such a course is futile according to Mises because what interventionism essentially aims to do is to contradict economic laws (e.g., the laws of demand and supply) by fiat. Secondly, Mises argues that the regulators must eventually realize that pursuing a policy of interventionism is indeed futile, but that by then the system will have become so chaotic, or that the exploitable private wealth to fund this policy (i.e., what Mises terms the “reserve fund”) will have been so depleted, that it will be too late to do anything except abandon the “middle way” of interventionism. The only internally consistent choices, Mises claims, are the extremes of laissez-faire capitalism or some form of pure collectivism, since moving toward any “mixed” system would still constitute interventionism and be subject to the same self-defeating forces.

Nonprice Regulation in an Industry

Standard analysis makes a sharp analytical distinction between price regulation on the one hand and nonprice regulation such as state-mandated, on-the-job safety regulations on the other. Price regulation, an unsupported price floor for instance, is seen to raise relative prices in such a way that, under conditions of perfect competition, the new equilibrium is associated with a surplus and deadweight losses.¹⁹ In contrast, nonprice regulations, which may also generate deadweight losses, are usually treated as essentially yet another cost of production; but because selling prices and quantities adjust to reflect this higher cost, the resulting equilibrium entails no disequilibrating shortage, even though output may have been reduced just as much as under a price floor (one unsupported by government, that is), and one could not say that relative prices have been distorted.

Job-safety regulations, however, will, to the extent that the regulation generates no positive externalities that can be captured by firms within the industry, *ceteris paribus* reduce the rate of return on investment in the industry. Labor and other productive resources will then tend to flow from the regulated industry into other industries with higher rates of return which, again *ceteris paribus*, will be those that are relatively less regulated. Hence, the unintended consequence of such regulations could very well be to distort the pattern of production and consumption from what it might have been otherwise. This result, however, is not unique to Austrian analysis. General-equilibrium theorizing would also go this far. Still, general-equilibrium analysis would not, indeed could not, appreciate the following consequence: namely, the erosion of property rights owing to such regulations *and* the resulting diminished reliability of relative prices in reflecting the expected demands of competing consumers. That is, to the extent that the capitalist is unable to control the resources that he nominally owns, his actions, in respect to trying to maximize the value of

his assets (e.g., by charging a price that tends to reflect his expectation of future demand and opportunity costs) will be compromised, and, as a result, the reliability of relative prices in reflecting relative scarcity will be lessened. Moreover, his incentive to be alert to new opportunities will be diminished to the extent that his economic ownership rights have been attenuated. Finally, nonprice regulations, by diminishing the pure profits that could be made through entrepreneurial discovery, impede the entrepreneurial adjustment of resources to changing conditions throughout the system. In a world that is ever outside of equilibrium, nonprice regulations can either mask genuine opportunities to align supply and demand or create “superfluous” opportunities for entrepreneurial profit (Kirzner 1985). Both outcomes are no less disordinating than the outcome under price regulation.

Income Transfers

The process by which interventions that attempt to equalize incomes by means of forced transfers is well known in the literature.²⁰ As in the case of nonprice regulation, however, less has been written on the resulting erosion of property rights and the consequent reduction in the effectiveness of (nonequilibrium) prices in signalling genuine error by means of entrepreneurial profit opportunities. Even less attention has been paid, in formal economic theory, to the impact of intervention on ideological preferences—i.e., the preference for extensions in state versus market power. As I argue elsewhere (Ikeda 1997), the disordinating effects of intervention through relative-price distortions, tends to be reinforced in the interventionist process by changes (both at the margin and through total shifts) in ideological preference. This effect is more central to the interventionist process in the case of income transfers than in pure economic regulation as, in Mises’s words, “It is a system that corrupts both givers and receivers” (1966:838). Note that rather than taking ideological preferences to be exogenous, which is the assumption of standard economics and political economy, this approach views them as being at least partly endogenous.

For example, not only will a publicly financed, guaranteed minimum income in the form of a monetary subsidy, under fairly general assumptions, tend to widen rather than narrow the gap between pretax and presubsidy incomes, the increased insecurity on the part of the “benefactors” (owing to diminished wealth and uncertainty over the value of what remains) and the reduced “moral aversion” to accepting handouts on the part of the beneficiaries (owing to the perception of political means as an increasingly popular and acceptable method of securing a living), will tend to increase each group’s demand for further intervention, either to extend the guarantee to a group of beneficiaries whose own security is weakened with every intervention or to lessen the dependency of beneficiaries on the perceived vagaries of the market.²¹ Unless an exogenous change in ideological preference takes place²² the expansion of state authority into the catallaxy will continue beyond the level deemed desirable by public choosers, precipitating a serious system-wide political-economic crisis.

Evaluating Robbery

Finally, with respect to theft, standard analysis presents its consequences strictly in terms of equilibrium outcomes. In typical textbook treatments (Landsburg 1995:271), for example,

one determines the equilibrium amount of theft by comparing the marginal cost and benefit of theft to the thief. Normatively, one would then measure the social cost of theft with reference to the deadweight loss (i.e., the difference between the value of the resources stolen to the legitimate owners and the thief). In addition, to prevent further loss of property, property owners will invest resources in alarms, locks, and other items that would, in the absence of robbery, be spent producing more highly valued goods.²³

From the perspective of political economy, however, an additional and proper concern for the analyst would also appear to be the impact of theft on the propensity to steal. That is, once again endogenous changes in preferences, at least in this case, ought to be an important part, not only of the practice of applying economic theory to the real world, but of political economic theory, itself.²⁴ Seen in this light, both the positive and normative economic impact of theft should really extend over time. It should encompass the future behavior of agents in the form of general patterns that economic theory would lead us to expect would emerge from the incentives (static and entrepreneurial) embedded in present behavior and institutions.

The links among different interventions through the unintended consequences of entrepreneurial adjustments in a world of radical ignorance is no better illustrated than in the case of theft and drug prohibition.²⁵ The prohibition of certain “recreational” drugs raises their relative prices, producing over time qualitative as well as quantitative changes in both the controlled product and in the behavior of buyers and sellers. It is true, of course, that the impact on the potency, quality, and safety of the prohibited drug, and, more importantly for our purposes, the apparently positive correlation between drug prices and crime is well understood by most economists. But in a neoclassical world of perfect information, including Public Choice, these linkages, at least insofar as policy analysts view them negatively, are hard to explain, for reasons that I have already discussed. That is, in a neoclassical world, would not perfectly informed policy (again, this may take the form of probabilities rather than point predictions) have already taken these dynamic effects into account *before* the implementation of drug prohibition? And if that is the case, would not these consequences necessarily be regarded as both expected and in some sense at least neutral?

The point, to reiterate, is not to deny that Public Choice, or any of the other varieties of neoclassical political economy, do not undertake the kind of analysis referred to here—such a claim would be empirically false. Rather, it is that in order to do so they must, at least tacitly, transcend the equilibrium framework from which they may have begun. And if we are to take theoretical consistency and the internal integrity of our analytical frameworks seriously, which will undoubtedly be necessary at some point in the progress of political economy, then it is essential that we acknowledge and effectively address the tension between Austrian interests and neoclassical method.

Conclusion

How then do we best address this problem? I cannot give a complete answer here. Yet, if we are interested in the kind of phenomena that I have associated with Austrian political economy—unintended consequences, linkages among interventions, endogenous changes in preference—then the first step would seem to be to explicitly transcend the equilibrium

framework of neoclassical theory.²⁶ This, I think, does not require completely abandoning the concept of equilibrium or even equilibrium analysis, but it does mean that our attention must be drawn away from statics to focus on processes. The explicit transcending of the equilibrium framework will make it clearer in which areas, specifically in theory development, we need to work to ground our intuitions about politico-economic processes on firm theoretical foundations. These would include such areas as theories of learning and learning failure, the dynamics of the mixed economy at the micro- and macro-levels, and the theory of the governmental process in terms more of limitations of knowledge rather than only of incentive problems.

At the moment, the most fruitful area for further theoretical research would appear to lie in marrying Austrian “error” and knowledge-problem considerations together with Public Choice’s starting point of “narrow political interest.” Such a marriage would be methodologically compatible since, as I argued earlier, the political-interest approach, while it appears to follow logically from an equilibrium, perfect-knowledge framework, does not itself entail such a framework.²⁷ Indeed, like the concept of (market or government) failure, itself, the whole notion of deception appears to make sense only in a world in which genuine error is possible. In any case, such a research program promises to benefit anyone who might be interested in understanding a wider range of actual politico-economic phenomena within a consistent unified framework.

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Notes

1. See Charles Rowley’s observations on the ideological compatibility between much of Public Choice and Austrian political economy. He notes that public-choice scholars (both Chicagoan and Virginian), “who have much in common in the field of ideology...derive their results through radically different scientific methods” (1994:288) from the Austrians. The present paper can be seen as an attempt to elaborate on the latter point.
2. The distinction between Virginia and Chicago Public Choice is also taken from Rowley (1994), and seems to be accepted, at least among the Virginians.
3. A recent issue of this journal (Volume 15, numbers 2/3) explored the common ground between Austrian Economics and Public Choice. The present article, in which I refer to several articles contained in that issue, can be seen as a continuation of that dialogue.
4. In particular, see Stiglitz (1994).
5. Standard references to the Austrian critique of neoclassical welfare economics are Rothbard (1956) and Kirzner (1973:212–242). For a more recent treatment see Cordato (1992).
6. That is, if transaction costs are sufficiently low, why don’t consumers and producers (of monopoly products, externalities, and public goods) bargain until social benefits and costs are equal at the margin? If they bargain only to the point that transaction costs permit, then the outcome must be optimal.
7. This point is made in Thomsen (1992).
8. Seen in this light, of course, the whole notion of “failure” in neoclassical economics becomes problematic.
9. Thus: “To the extent that [the equilibrium analysis of neoclassical economics] is influential, it runs counter to the broad thrust of Austrian economics...” (Rowley 1994:287).

10. In a ruthlessly consistent equilibrium analysis of this situation, it must be the case that some sort of transaction cost is preventing actors from bargaining away the deadweight loss and removing the deviation, so that the intervention is actually optimal. Donald Wittman (1995) appears to base his defense of interventionism from this position. Indeed, it is difficult to see what an effective public-choice critique of Wittman's position would be.) Moreover, deception would also be optimal, since presumably the cost to voters of being perfectly informed is too high at the margin, and once again it would be difficult to detect a genuine failure of any kind.
11. The linkages between these phenomena are discussed in particularly vivid detail (Murray 1984).
12. Wittman (1995) appears almost to take Public Choice to this extreme conclusion.
13. See Ikeda (1997) for an explanation for why government action will tend to produce frustrated intentions on net, while the market process will not.
14. Of course, when disagreement and compromise concerning the ends of a new law characterizes the actual legislative process, it may be difficult to identify just who the "supporters" are. This complication, however, would create very similar problems for both the Austrian and the public-choice approaches.
15. Elsewhere (Ikeda 1997:110–112) I explain the three meanings of "frustrated intentions" used in the Austrian political economy.
16. For obvious reasons, from an Austrian perspective, the "middle" would not include the upper-right quadrant, since perfect information is there considered an unrealistically extreme position.
17. Thus, Rowley informs us that while Virginia Public Choice "does not as frequently [as Chicago Public Choice] assume that the future should be analyzed in terms of risk rather than Knightian uncertainty...it does not regularly analyse political markets from the perspective of disequilibrium, nor does it employ the radical subjectivism of the Austrian school in its analysis of Public Choice" (1994:288).
18. The case for this influence is made clearly by Sutter (2002:200): "VPE [Virginia political economy] I argue has been influenced by Austrian economics' process view of the market economy."
19. These naturally depend on the price at which the surplus is disposed of. Under perfect information, producers would never produce the surplus unless someone (such as the government) offers a price support by guaranteeing to buy the surplus at the prevailing market price. If unsupported, the price floor will actually reduce planned output with respect to what equilibrium output would be in the absence of price control.
20. For an excellent discussion see Wagner (1989:89–106). See also Ikeda (1997:169–174).
21. See Ikeda (1997:176–186) for a detailed explanation of this process, which differentiates three distinct dynamic forces that operate to produce endogenous ideological change. The basis of this explanation is in Hayek (1944).
22. In Ikeda (1997) this occurs when public choosers finally make the connection between frustrated intentions, policy failure, and the doctrine of interventionism, which, however, requires a creative act of discovery. It is there argued that the conditions for this kind of discovery is most ripe only after an extensive amount of intervention has already taken place, especially after a profound crisis has shaken the entire system.
23. Note, however, that, on strictly neoclassical grounds, the amount invested in security against robbery is in fact optimal *given* the existence of robbery.
24. Although they were writing about incorporating dynamics into one's theoretical structure, the preceding comment in the text is in the spirit of O'Driscoll and Rizzo (1985).
25. For a thorough discussion of prohibition from an Austrian perspective, see Thornton (1991).
26. Benson (2002), Holcombe (2002), and Sutter (2002) are excellent examples of movements in such a direction.
27. The assumption of benevolence and public spiritedness on the part of public choosers is primarily a methodological assumption to help isolate the effects of partial radical ignorance on the interventionist process from those of narrow self-interest. It is secondarily a means of attributing good intentions to one's opponent in order to carry on constructive dialogue. As a description of hard political reality it is obviously only partially accurate, but that is not its role. I have stated this explicitly in Ikeda (1997), especially pp. 13, 145–151, and 234, where I have suggested that a marriage of Public Choice and Austrian political economy would be a significant step in the direction of a "general theory of political economy" (Ibid.:150) (hence the subtitle of my book, "Toward a Theory of Interventionism"). It is therefore curious that Boettke and Lopez (2002) should take this as a sign of APE being "methodologically inconsistent" with Public Choice, citing my work as a reference. First, the benevolence assumption is one that could be easily relaxed in APE. Second, although Benson (2002:253, n8) intriguingly suggests that some APE conclusions would have to be modified if narrow self-interest were integrated into the framework of interventionist analysis, as I have attempted to show here, the more profound methodological inconsistency lies in the assumption of perfect knowledge and equilibrium.

Boettke and Lopez's call for "a combined Austrian-public choice approach to political economy" that would relax both assumptions of omniscience and benevolence, thus repeats one of the major pleas of Ikeda (1997).

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