

HUMAN ACTION

by Ludwig von Mises, 4th edition (1996)

PART FOUR

CATALLACTICS OR ECONOMICS OF THE MARKET SOCIETY

XVI. PRICES, §§ 8-15

8. Monopoly of Demand

Monopoly prices can emerge only from a monopoly of supply. A monopoly of demand does not bring about a market situation different from that under not monopolized demand. The monopolist buyer--whether he is an individual or a group of individuals acting in concert--cannot reap a specific gain corresponding to the monopoly gains of monopolistic sellers. If he restricts demand, he will buy at a lower price. But then the quantity bought will drop too.

In the same way in which governments restrict competition in order to improve the position of privileged sellers, they can also restrict competition for the benefit of privileged buyers. Again and again governments have put an embargo on the export of certain commodities. Thus by excluding foreign buyers they have aimed at lowering the domestic price. But such a lower price is not a counterpart of monopoly prices.

What is commonly dealt with as monopoly of demand are certain phenomena of the determination of prices for specific complementary factors of production.

The production of one unit of the commodity m requires, besides the employment of various nonspecific factors, the employment of one unit of each of the two absolutely specific factors a and b . Neither a nor b can be replaced by any other factor; on the other hand a is of no use when not combined with b and vice versa. The available supply of a by far exceeds the available supply of b . It is therefore not possible for the owners of a to attain any price for a . The demand for a is always lags behind the supply; a is not an economic good. If a is a mineral deposit the extraction of which requires the use of capital and labor, the ownership of the deposits does not yield a royalty. There is no mining rent.

But if the owners of *a* form a cartel, they can turn the tables. They can restrict the supply of *a* offered for sale to such a fraction that the supply of *b* exceeds the supply of *a*. Now *a* becomes an economic good for which prices are paid while the price of *b* dwindles to zero. If then the owners of *b* react by forming a cartel too, a price struggle develops between the two monopolistic combines about the outcome of which catallactics can make no statements. As has already been pointed out, the pricing process does not bring about a uniquely determined result in cases in which more than one of the factors of production required is of an absolutely specific character.

It does not matter whether or not the market situation is such that the factors *a* and *b* together could be sold at monopoly prices. It does not make any difference whether the price for a lot including one unit of both *a* and *b* is a monopoly price or a competitive price.

Thus what is sometimes viewed as a monopoly of demand turns out to be a monopoly of supply formed under particular conditions. The sellers of *a* and *b* are intent upon selling at monopoly prices without regard to the question whether or not the price of *m* can become a monopoly price. What alone matters for them is to obtain as great a share as possible of the joint price which the buyers are ready to pay for *a* and *b* together. The case does not indicate any feature which would make it permissible to apply to it the term *monopoly of demand*. This mode of expression becomes understandable, however, if one takes into account the accidental features marking the contest between the two groups. If the owners of *a* (or *b*) are at the same time the entrepreneurs conducting the processing of *m*, their cartel takes on the outward appearance of a monopoly of demand. But this personal union combining two separate catallactic functions does not alter the essential issue; what is at stake is the settlement of affairs between two groups of monopolistic sellers.

Our example fits, *mutatis mutandis*, the case in which *a* and *b* can also be employed for purposes other than the production of *m*, provided these other employments only yield smaller returns.

9. Consumption as Affected by Monopoly Prices

The individual consumer may react to monopoly prices in different ways.

1. Notwithstanding the rise in price, the individual consumer does not restrict his purchases of the monopolized article. He prefers to restrict the purchase of other goods. (If all consumers were to react in this way, the

competitive price would have already risen to the height of the monopoly price.)

2. The consumer restricts his purchase of the monopolized article to such an extent that he does not spend for it more than he would have spent--for the purchase of a larger quantity--under the competitive price. (If all people were to react in this way, the seller would not get more under the monopoly price than he did under the competitive price; he would not derive any gain by deviating from the competitive price.)

3. The consumer restricts his purchase of the monopolized commodity to such an extent that he spends less for it than he would have spent under the competitive price; he buys with the money thus saved goods which he would not have bought otherwise. (If all people were to react in this way, the seller would harm his interests by substituting a higher price for the competitive price; no monopoly price could emerge. Only a benefactor who wanted to wean his fellow men from the consumption of pernicious drugs would in this case raise the price of the article concerned above the competitive level.)

4. The consumer spends more for the monopolized commodity than he would have spent under the competitive price and acquires only a smaller quantity of it.

However the consumer may react, his satisfaction appears to be impaired from the viewpoint of his own valuations. He is not so well served under monopoly prices as under competitive prices. The monopoly gain of the seller is borne by a monopoly deprivation of the buyer. Even if some consumers (as in case 3) acquire goods which they would not have bought in the absence of the monopoly price, their satisfaction is lower than it would have been under a different state of prices. Capital and labor which are withdrawn from the production of products which drops on account of the monopolistic restriction of the supply of one of the complementary factors required for their production, are employed for the production of other things which would otherwise not have been produced. But the consumers value these other things less.

Yet there is an exception to this general rule that monopoly prices benefit the seller and harm the buyer and infringe the supremacy of the consumers' interests. If on a competitive market one of the complementary factors, namely f , needed for the production of the consumers' good g , does not attain any price at all, although the production of f requires various expenditures and consumers are ready to pay for the consumers' good g a price which makes its production

profitable on a competitive market, the monopoly price for f becomes a necessary requirement for the production of g . It is this idea that people advance in favor of patent and copyright legislation. If inventors and authors were not in a position to make money by inventing and writing, they would be prevented from devoting their time to these activities and from defraying the costs involved. The public would not derive any advantage from the absence of monopoly prices for f . It would, on the contrary, miss the satisfaction it could derive from the acquisition of g .¹

Many people are alarmed by the reckless use of the deposits of minerals and oil which cannot be replaced. Our contemporaries, they say, squander an exhaustible stock without any regard for the coming generations. We are consuming our own birthright and that of the future. Now these complaints make little sense. We do not know whether later ages will still rely upon the same raw materials on which we depend today. It is true that the exhaustion of the oil deposits and even those of coal is progressing at a quick rate. But it is very likely that in a hundred or five hundred years people will resort to other methods of producing heat and power. Nobody knows whether we, in being less profligate with these deposits, would not deprive ourselves without any advantage to men of the twenty-first or of the twenty-fourth centuries. It is vain to provide for the needs of ages the technological abilities of which we cannot even dream.

But it is contradictory if the same people who lament the depletion of some natural resources are no less vehement in indicting monopolistic restraint in their present-day exploitation. The effect of monopoly prices of mercury is certainly a slowing down of the rate of depletion. In the eyes of those frightened by the aspect of a future scarcity of mercury this effect must appear highly desirable.

Economics in unmasking such contradictions does not aim at a "justification" of monopoly prices for oil, minerals, and ore. Economic has neither the task of justifying nor of condemning. It has merely to scrutinize the effects of all modes of human action. It does not enter the arena in which friends and foes of monopoly prices are intent upon pleading their causes.

Both sides in this heated controversy resort to fallacious arguments. The antimonopoly party is wrong in attributing to every monopoly the power to impair the situation of the buyers by restricting supply and bringing about monopoly prices. It is no less wrong in assuming that there prevails

¹ See below, pp. 680-681.

within a market economy, not hampered and sabotaged by government interference, a general tendency toward the formation of monopoly. It is a grotesque distortion of the true state of affairs to speak of *monopoly capitalism* instead of *monopoly interventionism* and of *private cartels* instead of *government-made cartels*. Monopoly prices would be limited to some minerals which can be mined in only a few places and to the field of local limited-space monopolies if the governments were not intent upon fostering them.²

The promonopoly party is wrong in crediting to the cartels the economics of big-scale production. Monopolistic concentration of production on one hand, they say, as a rule reduces average costs of production and thus increases the amount of capital and labor available for additional production. However, no cartel is needed in order to eliminate the plants producing at higher costs. Competition on the free market achieves this effect in the absence of any monopoly and of any monopoly prices. It is, on the contrary, often the purpose of government-sponsored cartelization to preserve the existence of plants and farms which the free market would force to discontinue operations precisely because they are producing at too high costs of production. The free market would have eliminated, for example, the submarginal farms and preserved only those for which production pays under the prevailing market price. But the New Deal preferred a different arrangement. It forced all farmers to a proportional restriction of output. It raised by its monopolistic policy the price of agricultural products to such a height that production became reasonable again on submarginal soil.

No less erroneous are the conclusions derived from a confusion of the economies of product standardization and monopoly. If men asked only for one standard type of a definite commodity, production of some articles could be arranged in a more economical way and costs would be lowered accordingly. But if people were to behave in such a manner, standardization and the corresponding cost reduction would emerge also in the absence of monopoly. If, on the other hand, one *forces* the consumers to be content with one standard type only, one does not increase their satisfaction; one impairs it. A dictator may deem the conduct of the consumers rather foolish. Why should they be so crazy about individually fashioned clothes? He may be right from the point of view of his own value judgments. But the trouble is that valuation is personal, individual, and arbitrary. The democracy of the market consists in the fact that people themselves make their choices and that no dictator has the power to force them to submit to his value judgments.

² See above, p. 366.

10. Price Discrimination on the Part of the Seller

Both competitive prices and monopoly prices are the same for all buyers. There prevails on the market a permanent tendency to eliminate all discrepancies in prices for the same commodity or service. Although the valuations of the buyers and the intensity of their demand as effective on the market are different, they pay the same prices. The wealthy man does not pay more for bread than the less wealthy man, although he would be ready to pay a higher price if he could not buy it cheaper. The enthusiast who would rather restrict his consumption of food than miss a performance of a Beethoven symphony pays no more for admission than a man for whom music is merely a pastime and who would not care for the concert if he could attend it only by renouncing his desire for some trifles. The difference between the price one must pay for a good and the highest amount one would be prepared to pay for it has sometimes been called consumers' surplus.³

But there can appear on the market conditions which make it possible for the seller to discriminate between the buyers. He can sell a commodity or a service at different prices to different buyers. He can obtain prices which may sometimes even rise to the point at which the whole consumers' surplus of a buyer disappears. Two conditions must coincide in order to make price discrimination advantageous to the seller.

The first condition is that those buying at a cheaper price are not in a position to resell the commodity or the service to people to whom the discriminating seller sells only at a higher price. If such reselling cannot be prevented, the first seller's intention would be thwarted. The second condition is that the public does not react in such a way that the total net proceeds of the seller lag behind the total net proceeds he would obtain under price uniformity. This second condition is always present under conditions which would make it advantageous to a seller to substitute monopoly prices for competitive prices. But it can also appear under a market situation which would not bring about monopoly gains. For price discrimination does not enjoin upon the seller the necessity of restricting the amount sold. He does not lose any buyer completely; he must merely take into account that some buyers may restrict the amount of their purchases. But as a rule he has the opportunity to sell the remainder of his supply to people who would not have bought at all or would have bought only smaller quantities if they had had to pay the uniform competitive price.

³ Cf. A. Marshall, *Principles of Economics* (8th ed. London, 1930), pp. 124-127.

Consequently the configuration of production costs plays no role in the considerations of the discriminating seller. Production costs are not affected as the total amount produced and sold remains unaltered.

The most common case of price discrimination is that of physicians. A doctor who can perform 80 treatments in a week and charges \$3 for each treatment is fully employed by attending to 30 patients and makes \$240 a week. If he charges the 10 wealthiest patients, who together consume 50 treatments, \$4 instead of \$3, they will consume only 40 treatments. The doctor sells the remaining 10 treatments at \$2 each to patients who would not have expended \$3 for his professional services. Then his weekly proceeds rise to \$270.

As price discrimination is practiced by the seller only if it is more advantageous to him than selling at a uniform price, it is obvious that it results in an alteration of consumption and the allocation of factors of production to various employments. The outcome of discrimination is always that the total amount expended for the acquisition of the good concerned increases. The buyers must provide for their excess expenditure by cutting down other purchases. As it is very unlikely that those benefitted by price discrimination will spend their gains for the purchase of the same goods as those the other people no longer buy in the same quantity, changes in the market data and in production become unavoidable.

In the above example the 10 wealthiest patients are damaged; they pay \$4 for a service for which they used to pay only \$3. But it is not only the doctor who derives advantage from the discrimination; the patients whom he charges \$2 are benefitted too. It is true they must provide the doctor's fees by renouncing other satisfactions. However, they value these other satisfactions less than that conveyed to them by the doctor's treatment. Their degree of contentment attained is increased.

For a full comprehension of price discrimination it is well to remember that, under the division of labor, competition among those eager to acquire the same product does not necessarily impair the individual competitor's position. The competitors' interests are antagonistic only with regard to the services rendered by the complementary nature-given factors of production. This inescapable natural antagonism is superseded by the advantages derived from the division of labor. As far as average costs of production can be reduced by big-scale production, competition among those eager to acquire the same commodity brings about an improvement in the individual competitor's situation. The fact that not

only a few people but a great number are eager to acquire the commodity c makes it possible to manufacture it in cost-saving processes; then even people with modest means can afford it. In the same way it can sometimes happen that price discrimination renders the satisfaction of a need possible which would have remained unsatisfied in its absence.

There live in a city p lovers of music, each of whom would be prepared to spend \$2 for the recital of a virtuoso. But such a concert requires an expenditure greater than $2p$ dollars and can therefore not be arranged. But if discrimination of admission fees is possible and among the p friends of music n are ready to spend \$4, the recital becomes feasible, provided that the amount $2(n + p)$ dollars is sufficient. Then n people spend \$4 each and $(p - n)$ people \$2 each for the admission and forego the satisfaction of the least urgent need they would have satisfied if they had not preferred to attend the recital. Each person in the audience fares better than he would have if the unfeasibility of price discrimination had prevented the performance. It is to the interest to the organizers to enlarge the audience to the point at which the admission of additional customers involves higher costs than the fees they are ready to spend.

Things would be different if the recital could have been arranged even if no more than \$2 was charged for admission. Then price discrimination would have impaired the satisfaction of those who are charged \$4.

The most common practices in selling admission tickets for artistic performances and railroad tickets at different rates are not the outcome of price discrimination in the catallactic sense of the term. He who pays a higher rate gets something appreciated more than he who pays less. He gets a better seat, a more comfortable traveling opportunity, and so on. Genuine price discrimination is present in the case of physicians who, although attending to each patient with the same care, charge the wealthier clients more than the less wealthy. It is present in the case of railroads charging more for the shipping of goods the transportation of which adds more to their value than for others although the costs incurred by the railroad are the same. It is obvious that both the doctor and the railroad can practice discrimination only within the limits fixed by the opportunity given to the patient and the shipper to find another solution of their problems that is more to their advantage. But this refers to one of the two conditions required for the emergence of price discrimination.

It would be idle to point out a state of affairs in which price discrimination could be practiced by all sellers of all kinds of commodities and services. It is more important to establish the fact that

within a market economy not sabotaged by government interference the conditions required for price discrimination are so rare that it can fairly be called an exceptional phenomenon.

11. Price Discrimination on the Part of the Buyer

While monopoly prices and monopoly gains cannot be realized to the advantage of a monopolistic buyer, the case is different with price discrimination. There is only one condition required for the emergence of price discrimination on the part of a monopolistic buyer on a free market, namely, crass ignorance of the state of the market on the part of the sellers. As such ignorance is unlikely to last for any length of time, price discrimination can only be practiced if the government interferes.

The Swiss Government has established a government owned and operated trade monopoly for cereals. It buys cereals at world-market prices on foreign markets and at higher prices from domestic farmers. In domestic purchases it pays a higher price to farmers producing at higher costs on the rocky soil of the mountain districts and a lower price--although still higher than the world-market price--to the farmers tilling more fertile land.

12. The Connexity of Prices

If a definite process of production brings about the products p and q simultaneously, the entrepreneurial decisions and actions are directed by weighing the sum of the anticipated prices of p and q . The prices of p and q are particularly connected with one another as changes in the demand for p (or for q) generate changes in the supply of q (or for p). The mutual relation of the prices of p and q can be called connexity of production. The businessman calls p (or q) a by-product of q (or p).

The production of the consumers' good z requires the employment of the factors p and q , the production of p the employment of the factors a and b , and the production of q the employment of the factors c and d . Then changes in the supply of p (or for q) bring about changes in the demand for q (or for p). It does not matter whether the process of producing z out of p and q is accomplished by the same enterprises which produce p out of a and b and q out of c and d , or by entrepreneurs financially independent of one another, or by the consumers themselves as a preliminary step in their consuming. The prices of p and q are particularly connected with one another because p is useless or of a smaller utility without q and vice versa. The mutual relation of the prices of p and q can be called connexity of consumption.

If the services rendered by a commodity *b* can be substituted, even though in a not perfectly satisfactory way, for those rendered by another commodity *a*, a change in the price of one of them affects the price of the other too. The mutual relation of the prices of *a* and *b* can be called connexity of substitution.

Connexity of production, connexity of consumption, and connexity of substitution are particular connexities of the prices of a limited number of commodities. From these particular connexities one must distinguish the general connexity of the prices of all goods and services. This general connexity is the outcome of the fact that for every kind of want-satisfaction, besides various more or less specific factors, one scarce factor is required which, in spite of the differences in its qualitative power to produce, can, within the limits precisely defined above⁴, be called a nonspecific factor--namely, labor.

Within a hypothetical world in which all factors of production are absolutely specific, human action would operate in a multiplicity of fields of want-satisfaction independent of one another. What links together in our actual world the various fields of want-satisfaction is the existence of a great many nonspecific factors, suitable to be employed for the attainment of various ends and to be substituted in some degree for one another. The fact that *one* factor, labor, is on the one hand required for every kind of production and on the other hand is, within the limits defined, nonspecific, brings about the general connexity of all human activities. It integrates the pricing process into a whole in which all gears work on one another. It makes the market a concatenation of mutually interdependent phenomena.

It would be absurd to look upon a definite price as if it were an isolated object in itself. A price is expressive of the position which acting men attach to a thing under the present state of their efforts to remove uneasiness. It does not indicate a relationship to something unchanging, but merely the instantaneous position in a kaleidoscopically changing assemblage. In this collection of things considered valuable by the value judgments of acting men each particle's place is interrelated with those of all other particles. What is called a price is always a relationship within an integrated system which is the composite effect of human relations.

13. Prices and Income

⁴ Cf. above, pp. 133-135.

A market price is a real historical phenomenon, the quantitative ratio at which at a definite place and at a definite date two individuals exchanged definite quantities of two definite goods. It refers to the special conditions of the concrete act of exchange. It is ultimately determined by the value judgments of the individuals involved. It is not derived from the general price structure or from the structure of the prices of a special class of commodities or services. What is called the price structure is an abstract notion derived from a multiplicity of individual concrete prices. The market does not generate prices of land or motorcars in general nor wage rates in general, but prices for a certain piece of land and for a certain car and wage rates for a performance of a certain kind. It does not make any difference for the pricing process to what class the things exchanged are to be assigned from any point of view. However they may differ in other regards, in the very act of exchange they are nothing but commodities, i.e., things valued on account of their power to remove felt uneasiness.

The market does not create or determine incomes. It is not a process of income formation. If the owner of a piece of land and the worker husband the physical resources concerned, the land and the man will renew and preserve their power to render services; the agricultural and urban land for a practically indefinite period, the man for a number of years. If the market situation for these factors of production does not deteriorate, it will be possible in the future too to attain a price for their productive employment. Land and working power can be considered as sources of income if they are dealt with as such, that is, if their capacity to produce is not prematurely exhausted by reckless exploitation. It is provident restraint in the use of factors of production, not their natural and physical properties, which convert them into somewhat durable sources of income. There is in nature no such thing as a stream of income. Income is a category of action; it is the outcome of careful economizing of scarce factors. This is still more obvious in the case of capital goods. The produced factors of production are not permanent. Although some of them may have a life of many years, all of them eventually become useless through wear and tear, sometimes even by the mere passing of time. They become durable sources of income only if their owners treat them as such. Capital can be preserved as a source of income if the consumption of its products, market conditions remaining unchanged, is restricted in such a way as not to impair the replacement of the worn out parts.

Changes in the market data can frustrate every endeavor to perpetuate a source of income. Industrial equipment becomes obsolete if demand changes or if it is superseded by something better. Land becomes useless

if more fertile soil is made accessible in sufficient quantities. Expertness and skill for the performance of special kinds of work lose their remunerativeness when new fashions or new methods of production narrow the opportunity for their employment. The success of any provision for the uncertain future depends on the correctness of the anticipations which guided it. No income can be made safe against changes not adequately foreseen.

Neither is the pricing process a form of distribution. As has been pointed out already, there is nothing in the market economy to which the notion of distribution could be applied.

14. Prices and Production

The pricing process of the unhampered market directs production into those channels in which it best serves the wishes of the consumers as manifested on the market. Only in the case of monopoly prices have the monopolists the power to divert production, within a limited range, from this line into other lines to their own benefit.

The prices determine which of the factors of production should be employed and which should be left unused. The specific factors of production are employed only if there is no more valuable employment available for the complementary nonspecific factors. There are technological recipes, land, and nonconvertible capital goods whose capacity to produce remains unused because their employment would mean a waste of the scarcest of all factors, labor. While under the conditions present in our world there cannot be in the long run unemployment of labor in a free labor market, unused capacity of land and of inconvertible industrial equipment is a regular phenomenon.

It is nonsense to lament the fact of unused capacity. The unused capacity of equipment made obsolete by technological improvement is a landmark of material progress. It would be a blessing if the establishment of durable peace would render munitions plants unused or if the discovery of an efficient method of preventing and curing tuberculosis would render obsolete sanatoria for the treatment of people affected by this evil. It would be sensible to deplore the lack of provision in the past which resulted in malinvestment of capital goods. Yet, men are not infallible. A certain amount of malinvestment is unavoidable. What has to be done is to shun policies that like credit expansion artificially foster malinvestment.

Modern technology could easily grow oranges and grapes in hot-houses in the arctic and subarctic countries. Everybody would call such a venture lunacy. But it is essentially the same to preserve the growing of cereals in rocky mountain valleys by tariffs and other devices of protectionism while elsewhere there is plenty of fallow fertile land. The difference is merely one of degree.

The inhabitants of the Swiss Jura prefer to manufacture watches instead of growing wheat. Watchmaking is for them the cheapest way to acquire wheat. On the other hand the growing of wheat is the cheapest way for the Canadian farmer to acquire watches. The fact that the inhabitants of the Jura do not grow wheat and the Canadians do not manufacture watches is not more worthy of notice than the fact that tailors do not make their shoes and shoemakers do not make their clothes.

15. The Chimera of Nonmarket Prices

Prices are a market phenomenon. They are generated by the market process and are the pith of the market economy. There is no such thing as prices outside the market. Prices cannot be constructed synthetically, as it were. They are the resultant of a certain constellation of market data, of actions and reactions of the members of a market society. It is vain to meditate what prices would have been if some of their determinants had been different. Such fantastic designs are no more sensible than whimsical speculations about what the course of history would have been if Napoleon had been killed in the battle of Arcole or if Lincoln had ordered Major Anderson to withdraw from Fort Sumter.

It is no less vain to ponder on what prices ought to be. Everybody is pleased if the prices of things he wants to buy drop and the prices of the things he wants to sell rise. In expressing such wishes a man is sincere if he admits that his point of view is personal. It is another question whether, from his personal point of view, he would be well advised to prompt the government to use its power of coercion and oppression to interfere with the market's price structure. It will be shown in the sixth part of this book what the inescapable consequences of such a policy of interventionism must be.

But one deludes oneself or practices deception if one calls such wishes and arbitrary value judgments the voice of objective truth. In human action nothing counts but the various individuals' desires for the attainment of ends. With regard to the choice of these ends there is no question of truth; all that matters is value. Value judgments are

necessarily always subjective, whether they are passed by one man only or by many men, by a blockhead, a professor, or a statesman.

Any price determined on a market is the necessary outgrowth of the interplay of the forces operating, that is, demand and supply. Whatever the market situation which generated this price may be, with regard to it the price is always adequate, genuine, and real. It cannot be higher if no bidder ready to offer a higher price turns up, and it cannot be lower if no seller ready to deliver at a lower price turns up. Only the appearance of such people ready to buy or to sell can alter prices.

Economics analyzes the market process which generates commodity prices, wage rates, and interest rates. It does not develop formulas which would enable anybody to compute a "correct" price different from that established on the market by the interaction of buyers and sellers.

At the bottom of many efforts to determine nonmarket prices is the confused and contradictory notion of real costs. If costs were a real thing, i.e., a quantity independent of personal value judgments and objectively discernible and measurable, it would be possible for a disinterested arbiter to determine their height and thus the correct price. There is no need to dwell any longer on the absurdity of this idea. Costs are a phenomenon of valuation. Costs are the value attached to the most valuable want-satisfaction which remains unsatisfied because the means required for its satisfaction are employed for that want-satisfaction the cost of which we are dealing with. The attainment of an excess of the value of the product over the costs, a profit, is the goal of every production effort. Profit is the pay-off of successful action. It cannot be defined without reference to valuation. It is a phenomenon of valuation and has no direct relation to physical and other phenomena of the external world.

Economic analysis cannot help reducing all items of cost to value judgments. The socialists and interventionists call entrepreneurial profit, interest on capital, and rent of land "unearned" because they consider that only the toil and trouble of the worker is real and worthy of being rewarded. However, reality does not reward toil and trouble. If toil and trouble is expended according to well-conceived plans, its outcome increases the means available for want-satisfaction. Whatever some people may consider as just and fair, the only relevant question is always the same. What alone matters is which system of social organization is better suited to attain those ends for which people are ready to expend toil and trouble. The question is: market economy, or socialism? There is no third solution. The notion of a market economy with nonmarket prices is

absurd. The very idea of cost prices is unrealizable. Even if the cost price formula is applied only to entrepreneurial profits, it paralyzes the market. If commodities and services are to be sold below the price the market would have determined for them, supply always lags behind demand. Then the market can neither determine what should or should not be produced, nor to whom the commodities and services should go. Chaos results.

This refers also to monopoly prices. It is reasonable to abstain from all policies which could result in the emergence of monopoly prices. But whether monopoly prices are brought about by such promonopoly government policies or in spite of the absence of such policies, no alleged "fact finding" and no armchair speculation can discover another price at which demand and supply would become equal. The failure of all experiments to find a satisfactory solution for the limited-space monopoly of public utilities clearly proves this truth.

It is the very essence of prices that they are the offshoot of the actions of individuals and groups of individuals acting on their own behalf. The catallactic concept of exchange ratios and prices precludes anything that is the effect of actions of a central authority, of people resorting to violence and threats in the name of society or the state or of an armed pressure group. In declaring that it is not the business of the government to determine prices, we do not step beyond the borders of logical thinking. A government can no more determine prices than a goose can lay hen's eggs.

We can think of a social system in which there are no prices at all, and we can think of government decrees which aim at fixing prices at a height different from that which the market would determine. It is one of the tasks of economics to study the problems implied. However, precisely because we want to examine these problems it is necessary clearly to distinguish between prices and government decrees. Prices are by definition determined by peoples' buying and selling or abstention from buying and selling. They must not be confused with fiats issued by governments or other agencies enforcing their orders by an apparatus of coercion and compulsion.⁵

⁵ In order not to confuse the reader by the introduction of too many new terms, we shall keep to the widespread usage of calling such fiats *prices, interest rates, wage rates decreed and enforced by governments or other agencies of compulsion (e.g., labor unions)*. But one must never lose sight of the fundamental difference between the market phenomena of prices, wages, and interest rates on the one hand, and the legal phenomena of maximum or minimum prices, wages, and interest rates, designed to nullify these market phenomena, on the other hand.