



Classical Economics

An Austrian Perspective on
the History of Economic Thought

Volume II

Murray N. Rothbard

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To my mentors,
Ludwig von Mises and Joseph Dorfman

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Ludwig
von Mises
Institute

AUBURN, ALABAMA



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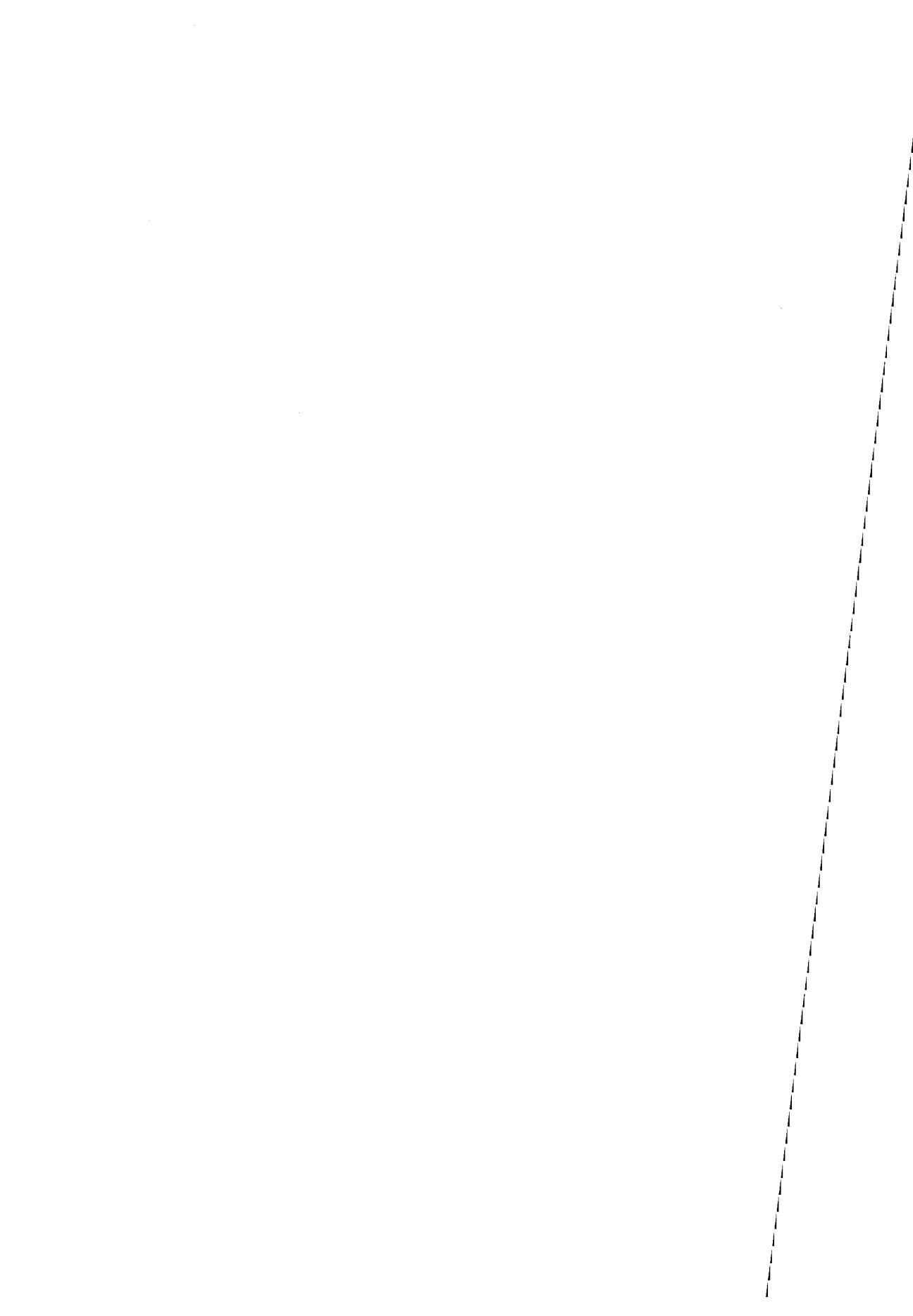
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Introduction

As the subtitle declares, this work is an overall history of economic thought from a frankly ‘Austrian’ standpoint: that is, from the point of view of an adherent of the ‘Austrian School’ of economics. This is the only such work by a modern Austrian; indeed, only a few monographs in specialized areas of the history of thought have been published by Austrians in recent decades.¹ Not only that: this perspective is grounded in what is currently the least fashionable though not the least numerous variant of the Austrian School: the ‘Misesian’ or ‘praxeologic’.²

But the Austrian nature of this work is scarcely its only singularity. When the present author first began studying economics in the 1940s, there was an overwhelmingly dominant paradigm in the approach to the history of economic thought – one that is still paramount, though not as baldly as in that era. Essentially, this paradigm features a few Great Men as the essence of the history of economic thought, with Adam Smith as the almost superhuman founder. But if Smith was the creator of both economic analysis and of the free trade, free market tradition in political economy, it would be petty and niggling to question seriously any aspect of his alleged achievement. Any sharp criticism of Smith as either economist or free market advocate would seem only anachronistic: looking down upon the pioneering founder from the point of view of the superior knowledge of today, puny descendants unfairly bashing the giants on whose shoulders we stand.

If Adam Smith created economics, much as Athena sprang full-grown and fully armed from the brow of Zeus, then his predecessors must be foils, little men of no account. And so short shrift was given, in these classic portrayals of economic thought, to anyone unlucky enough to precede Smith. Generally they were grouped into two categories and brusquely dismissed. Immediately preceding Smith were the mercantilists, whom he strongly criticized. Mercantilists were apparently boobs who kept urging people to accumulate money but not to spend it, or insisting that the balance of trade must ‘balance’ with each country. Scholastics were dismissed even more rudely, as moralistic medieval ignoramuses who kept warning that the ‘just’ price must cover a merchant’s cost of production plus a reasonable profit.

The classic works in the history of thought of the 1930s and 1940s then proceeded to expound and largely to celebrate a few peak figures after Smith. Ricardo systematized Smith, and dominated economics until the 1870s; then the ‘marginalists’, Jevons, Menger and Walras, marginally corrected Smith–

Ricardo ‘classical economics’ by stressing the importance of the marginal unit as compared to whole classes of goods. Then it was on to Alfred Marshall, who sagely integrated Ricardian cost theory with the supposedly one-sided Austrian–Jevonian emphasis on demand and utility, to create modern neoclassical economics. Karl Marx could scarcely be ignored, and so he was treated in a chapter as an aberrant Ricardian. And so the historian could polish off his story by dealing with four or five Great Figures, each of whom, with the exception of Marx, contributed more building blocks toward the unbroken progress of economic science, essentially a story of ever onward and upward into the light.³

In the post-World War II years, Keynes of course was added to the Pantheon, providing a new culminating chapter in the progress and development of the science. Keynes, beloved student of the great Marshall, realized that the old man had left out what would later be called ‘macroeconomics’ in his exclusive emphasis on the micro. And so Keynes added macro, concentrating on the study and explanation of unemployment, a phenomenon which everyone before Keynes had unaccountably left out of the economic picture, or had conveniently swept under the rug by blithely ‘assuming full employment’.

Since then, the dominant paradigm has been largely sustained, although matters have recently become rather cloudy. For one thing, this kind of Great Man ever-upward history requires occasional new final chapters. Keynes’s *General Theory*, published in 1936, is now almost sixty years old; surely there must be a Great Man for a final chapter? But who? For a while, Schumpeter, with his modern and seemingly realistic stress on ‘innovation’, had a run, but this trend came a cropper, perhaps on the realization that Schumpeter’s fundamental work (or ‘vision’, as he himself perceptively put it) was written more than two decades before the *General Theory*. The years since the 1950s have been murky; and it is difficult to force a return to the once-forgotten Walras into the Procrustean bed of continual progress.

My own view of the grave deficiency of the Few Great Men approach has been greatly influenced by the work of two splendid historians of thought. One is my own dissertation mentor Joseph Dorfman, whose unparalleled multi-volume work on the history of American economic thought demonstrated conclusively how important allegedly ‘lesser’ figures are in any movement of ideas. In the first place, the stuff of history is left out by omitting these figures, and history is therefore falsified by selecting and worrying over a few scattered texts to constitute The History of Thought. Second, a large number of the supposedly secondary figures contributed a great deal to the development of thought, in some ways more than the few peak thinkers. Hence, important features of economic thought get omitted, and the developed theory is made paltry and barren as well as lifeless.

Furthermore, the cut-and-thrust of history itself, the context of the ideas and movements, how people influenced each other, and how they reacted to

and against one another, is necessarily left out of the Few Great Men approach. This aspect of the historian's work was particularly brought home to me by Quentin Skinner's notable two-volume *Foundations of Modern Political Thought*, the significance of which could be appreciated without adopting Skinner's own behaviourist methodology.⁴

The continual progress, onward-and-upward approach was demolished for me, and should have been for everyone, by Thomas Kuhn's famed *Structure of Scientific Revolutions*.⁵ Kuhn paid no attention to economics, but instead, in the standard manner of philosophers and historians of science, focused on such ineluctably 'hard' sciences as physics, chemistry, and astronomy. Bringing the word 'paradigm' into intellectual discourse, Kuhn demolished what I like to call the 'Whig theory of the history of science'. The Whig theory, subscribed to by almost all historians of science, including economics, is that scientific thought progresses patiently, one year after another developing, sifting, and testing theories, so that science marches onward and upward, each year, decade or generation learning more and possessing ever more correct scientific theories. On analogy with the Whig theory of history, coined in mid-nineteenth century England, which maintained that things are always getting (and therefore must get) better and better, the Whig historian of science, seemingly on firmer grounds than the regular Whig historian, implicitly or explicitly asserts that 'later is always better' in any particular scientific discipline. The Whig historian (whether of science or of history proper) really maintains that, for any point of historical time, 'whatever was, was right', or at least better than 'whatever was earlier'. The inevitable result is a complacent and infuriating Panglossian optimism. In the historiography of economic thought, the consequence is the firm if implicit position that every individual economist, or at least every school of economists, contributed their important mite to the inexorable upward march. There can, then, be no such thing as gross systemic error that deeply flawed, or even invalidated, an entire school of economic thought, much less sent the world of economics permanently astray.

Kuhn, however, shocked the philosophic world by demonstrating that this is simply not the way that science has developed. Once a central paradigm is selected, there is no testing or sifting, and tests of basic assumptions only take place after a series of failures and anomalies in the ruling paradigm has plunged the science into a 'crisis situation'. One need not adopt Kuhn's nihilistic philosophic outlook, his implication that no one paradigm is or can be better than any other, to realize that his less than starry-eyed view of science rings true both as history and as sociology.

But if the standard romantic or Panglossian view does not work even in the hard sciences, *a fortiori* it must be totally off the mark in such a 'soft science' as economics, in a discipline where there can be no laboratory testing, and

where numerous even softer disciplines such as politics, religion, and ethics necessarily impinge on one's economic outlook.

There can therefore be no presumption whatever in economics that later thought is better than earlier, or even that all well-known economists have contributed their sturdy mite to the developing discipline. For it becomes very likely that, rather than everyone contributing to an ever-progressing edifice, economics can and has proceeded in contentious, even zig-zag fashion, with later systemic fallacy sometimes elbowing aside earlier but sounder paradigms, thereby redirecting economic thought down a total erroneous or even tragic path. The overall path of economics may be up, or it may be down, over any give time period.

In recent years, economics, under the dominant influence of formalism, positivism and econometrics, and preening itself on being a hard science, has displayed little interest in its own past. It has been intent, as in any 'real' science, on the latest textbook or journal article rather than on exploring its own history. After all, do contemporary physicists spend much time poring over eighteenth century optics?

In the last decade or two, however, the reigning Walrasian–Keynesian neoclassical formalist paradigm has been called ever more into question, and a veritable Kuhnian 'crisis situation' has developed in various areas of economics, including worry over its methodology. Amidst this situation, the study of the history of thought has made a significant comeback, one which we hope and expect will expand in coming years.⁶ For if knowledge buried in paradigms lost can disappear and be forgotten over time, then studying older economists and schools of thought need not be done merely for antiquarian purposes or to examine how intellectual life proceeded in the past. Earlier economists can be studied for their important contributions to forgotten and therefore new knowledge today. Valuable truths can be learned about the content of economics, not only from the latest journals, but from the texts of long-deceased economic thinkers.

But these are merely methodological generalizations. The concrete realization that important economic knowledge had been lost over time came to me from absorbing the great revision of the scholastics that developed in the 1950s and 1960s. The pioneering revision came dramatically in Schumpeter's great *History of Economic Analysis*, and was developed in the works of Raymond de Roover, Marjorie Grice-Hutchinson and John T. Noonan. It turns out that the scholastics were not simply 'medieval', but began in the thirteenth century and expanded and flourished through the sixteenth and into the seventeenth century. Far from being cost-of-production moralists, the scholastics believed that the just price was whatever price was established on the 'common estimate' of the free market. Not only that: far from being naive labour or cost-of-production value theorists, the scholastics may be consid-

ered ‘proto-Austrians’, with a sophisticated subjective utility theory of value and price. Furthermore, some of the scholastics were far superior to current formalist microeconomics in developing a ‘proto-Austrian’ dynamic theory of entrepreneurship. Moreover, in ‘macro’, the scholastics, beginning with Buridan and culminating in the sixteenth century Spanish scholastics, worked out an ‘Austrian’ rather than monetarist supply and demand theory of money and prices, including interregional money flows, and even a purchasing-power parity theory of exchange rates.

It seems to be no accident that this dramatic revision of our knowledge of the scholastics was brought to American economists, not generally esteemed for their depth of knowledge of Latin, by European-trained economists steeped in Latin, the language in which the scholastics wrote. This simple point emphasizes another reason for loss of knowledge in the modern world: the insularity in one’s own language (particularly severe in the English-speaking countries) that has, since the Reformation, ruptured the once Europe-wide community of scholars. One reason why continental economic thought has often exerted minimal, or at least delayed, influence in England and the United States is simply because these works had not been translated into English.⁷

For me, the impact of scholastic revisionism was complemented and strengthened by the work, during the same decades, of the German-born ‘Austrian’ historian, Emil Kauder. Kauder revealed that the dominant economic thought in France and Italy during the seventeenth and especially the eighteenth centuries was also ‘proto-Austrian’, emphasizing subjective utility and relative scarcity as the determinants of value. From this groundwork, Kauder proceeded to a startling insight into the role of Adam Smith that, however, follows directly from his own work and that of the scholastic revisionists: that Smith, far from being the founder of economics, was virtually the reverse. On the contrary, Smith actually took the sound, and almost fully developed, proto-Austrian subjective value tradition, and tragically shunted economics on to a false path, a dead end from which the Austrians had to rescue economics a century later. Instead of subjective value, entrepreneurship, and emphasis on real market pricing and market activity, Smith dropped all this and replaced it with a labour theory of value and a dominant focus on the unchanging long-run ‘natural price’ equilibrium, a world where entrepreneurship was assumed out of existence. Under Ricardo, this unfortunate shift in focus was intensified and systematized.

If Smith was not the creator of economic theory, neither was he the founder of *laissez-faire* in political economy. Not only were the scholastics analysts of, and believers in, the free market and critics of government intervention; but the French and Italian economists of the eighteenth century were even more *laissez-faire*-oriented than Smith, who introduced numerous waffles

and qualifications into what had been, in the hands of Turgot and others, an almost pure championing of *laissez-faire*. It turns out that, rather than someone who should be venerated as creator of modern economics or of *laissez-faire*, Smith was closer to the picture portrayed by Paul Douglas in the 1926 Chicago commemoration of the *Wealth of Nations*: a necessary precursor of Karl Marx.

Emil Kauder's contribution was not limited to his portrayal of Adam Smith as the destroyer of a previously sound tradition of economic theory, as the founder of an enormous 'zag' in a Kuhnian picture of a zig-zag history of economic thought. Also fascinating if more speculative was Kauder's estimate of the essential *cause* of a curious asymmetry in the course of economic thought in different countries. Why is it, for example, that the subjective utility tradition flourished on the Continent, especially in France and Italy, and then revived particularly in Austria, whereas the labour and cost of production theories developed especially in Great Britain? Kauder attributed the difference to the profound influence of religion: the scholastics, and then France, Italy and Austria were Catholic countries, and Catholicism emphasized consumption as the goal of production and consumer utility and enjoyment as, at least in moderation, valuable activities and goals. The British tradition, on the contrary, beginning with Smith himself, was Calvinist, and reflected the Calvinist emphasis on hard work and labour toil as not only good but a great good in itself, whereas consumer enjoyment is at best a necessary evil, a mere requisite to continuing labour and production.

On reading Kauder, I considered this view a challenging insight, but essentially an unproven speculation. However, as I continued studying economic thought and embarked on writing these volumes, I concluded that Kauder was being confirmed many times over. Even though Smith was a 'moderate' Calvinist, he was a staunch one nevertheless, and I came to the conclusion that the Calvinist emphasis could account, for example, for Smith's otherwise puzzling championing of usury laws, as well as his shift in emphasis from the capricious, luxury-loving consumer as the determinant of value, to the virtuous labourer embedding his hours of toil into the value of his material product.

But if Smith could be accounted for by Calvinism, what of the Spanish-Portuguese Jew-turned-Quaker, David Ricardo, surely no Calvinist? Here it seems to me that recent research into the dominant role of James Mill as mentor of Ricardo and major founder of the 'Ricardian system' comes strongly into play. For Mill was a Scotsmen ordained as a Presbyterian minister and steeped in Calvinism; the fact that, later in life, Mill moved to London and became an agnostic had no effect on the Calvinist nature of Mill's basic attitudes toward life and the world. Mill's enormous evangelical energy, his crusading for social betterment, and his devotion to labour toil (as well as the

cognate Calvinist virtue of thrift) reflected his lifelong Calvinist world-outlook. John Stuart Mill's resurrection of Ricardianism may be interpreted as his fileopietist devotion to the memory of his dominant father, and Alfred Marshall's trivialization of Austrian insights into his own neo-Ricardian schema also came from a highly moralistic and evangelical neo-Calvinist.

Conversely, it is no accident that the Austrian School, the major challenge to the Smith–Ricardo vision, arose in a country that was not only solidly Catholic, but whose values and attitudes were still heavily influenced by Aristotelian and Thomist thought. The German precursors of the Austrian School flourished, not in Protestant and anti-Catholic Prussia, but in those German states that were either Catholic or were politically allied to Austria rather than Prussia.

The result of these researches was my growing conviction that leaving out religious outlook, as well as social and political philosophy, would disastrously skew any picture of the history of economic thought. This is fairly obvious for the centuries before the nineteenth, but it is true for that century as well, even as the technical apparatus takes on more of a life of its own.

In consequence of these insights, these volumes are very different from the norm, and not just in presenting an Austrian rather than a neoclassical or institutionalist perspective. The entire work is much longer than most since it insists on bringing in all the ‘lesser’ figures and their interactions as well as emphasizing the importance of their religious and social philosophies as well as their narrower strictly ‘economic’ views. But I would hope that the length and inclusion of other elements does not make this work less readable. On the contrary, history necessarily means narrative, discussion of real persons as well as their abstract theories, and includes triumphs, tragedies, and conflicts, conflicts which are often moral as well as purely theoretical. Hence, I hope that, for the reader, the unwonted length will be offset by the inclusion of far more human drama than is usually offered in histories of economic thought.

Murray N. Rothbard
Las Vegas, Nevada

Notes

1. Joseph Schumpeter's valuable and monumental *History of Economic Analysis* (New York: Oxford University Press, 1954), has sometimes been referred to as ‘Austrian’. But while Schumpeter was raised in Austria and studied under the great Austrian Böhm-Bawerk, he himself was a dedicated Walrasian, and his *History* was, in addition, eclectic and idiosyncratic.
2. For an explanation of the three leading Austrian paradigms at the present time, see Murray N. Rothbard, *The Present State of Austrian Economics* (Auburn, Ala.: Ludwig von Mises Institute, 1992).
3. When the present author was preparing for his doctoral orals at Columbia University, he

- had the venerable John Maurice Clark as examiner in the history of economic thought. When he asked Clark whether he should read Jevons, Clark replied, in some surprise: 'What's the point? The good in Jevons is all in Marshall'.
4. Joseph Dorfman, *The Economic Mind in American Civilization* (5 vols, New York: Viking Press, 1946–59); Quentin Skinner, *The Foundations of Modern Political Thought* (2 vols, Cambridge: Cambridge University Press, 1978).
 5. Thomas S. Kuhn, *The Structure of Scientific Revolutions* (1962, 2nd ed., Chicago: University of Chicago Press, 1970).
 6. The attention devoted in recent years to a brilliant critique of neoclassical formalism as totally dependent on obsolete mid-nineteenth century mechanics is a welcome sign of this recent change of attitude. See Philip Mirowski, *More Heat than Light* (Cambridge: Cambridge University Press, 1989).
 7. At the present time, when English has become the European *lingua franca*, and most European journals publish articles in English, this barrier has been minimized.

Acknowledgements

These volumes were directly inspired by Mark Skousen, of Rollins College, Florida, who urged me to write a history of economic thought from an Austrian perspective. In addition to providing the spark, Skousen persuaded the Institute for Political Economy to support my research during its first academic year. Mark first envisioned the work as a standard Smith-to-the-present moderately sized book, a sort of contra-Heilbroner. After pondering the problem, however, I told him that I would have to begin with Aristotle, since Smith was a sharp decline from many of his predecessors. Neither of us realized then the scope or length of the ensuing research.

It is impossible to list all the persons from whom I have learned in a lifetime of instruction and discussion in the history of economics and all its cognate disciplines. Here I shall have to slight most of them and single out a few. The dedication acknowledges my immense debt to Ludwig von Mises for providing a mighty edifice of economic theory, as well as for his teaching, his friendship, and for the inspiring example of his life. And to Joseph Dorfman for his path-breaking work in the history of economic thought, his stress on the importance of the stuff of history as well as of the theories themselves, and his painstaking instruction in historical method.

I owe a great debt to Llewellyn H. Rockwell Jr for creating and organizing the Ludwig von Mises Institute, establishing it at Auburn University, and building it, in merely a decade, into a flourishing and productive centre for advancing and instructing people in Austrian economics. Not the least service to me of the Mises Institute was attracting a network of scholars from whom I could learn. Here again I must single out Joseph T. Salerno, of Pace University, who has done remarkably creative work in the history of economic thought; and that extraordinary polymath and scholar's scholar, David Gordon of the Mises Institute, whose substantial output in philosophy, economics and intellectual history embodies only a small fraction of his erudition in these and many other fields. Also thanks to Gary North, head of the Institute for Christian Economics in Tyler, Texas, for leads into the extensive bibliography on Marx and on socialism generally, and for instructing me in the mysteries of varieties of millennialism, a-, pre- and post. None of these people, of course, should be implicated in any of the errors herein.

Most of my research was conducted with the aid of the superb resources of Columbia and Stanford University libraries, as well as the library at the University of Nevada, Las Vegas, supplemented by my own book collection

accumulated over the years. Since I am one of the few scholars remaining who stubbornly cleave to low-tech typewriters rather than adopt word processors/computers, I have been dependent on the services of a number of typists/word processors, among whom I would particularly mention Janet Bunker and Donna Evans of the University of Nevada, Las Vegas.

1 J.B. Say: the French tradition in Smithian clothing

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1.1 The Smithian conquest of France

One of the great puzzles in the history of economic thought, as we have indicated, in Volume 1, is why Adam Smith was able to sweep the field and enjoy the reputation of ‘founder of economic science’ when Cantillon and Turgot had been far superior, both as technical economic analysts and as champions of *laissez-faire*. The mystery is particularly acute for France, since in Britain the only schools competing with the Smithians were the mercantilists and the political arithmeticians. The mystery deepens when we realize that the great leader of French economics after Smith, Jean-Baptiste Say (1767–1832), was *really* in the Cantillon–Turgot tradition rather than that of Smith even though he greatly neglected the former and proclaimed that economics began with Adam Smith. He, Say, was supposedly only systematizing the wonderful but inchoate truths found in the *Wealth of Nations*. We shall see below the precise nature of Say’s thought and his contributions, as well as his decidedly ‘French’ non-Smithian, and ‘pre-Austrian’ logical clarity and emphasis on the praxeologic axiomatic–deductive method, on utility as the sole source of economic value, on the entrepreneur, on the productivity of the factors of production, and on individualism.

Specifically, in his brief treatment of the history of thought in his great *Treatise on Political Economy*, Say makes no mention whatever of Cantillon. Despite the considerable influence of Turgot on his doctrine, he brusquely dismisses Turgot as sound on politics but of no account in economics, and asserts that political economy in effect began with Adam Smith’s *Wealth of Nations*. This curious and wilful neglect of his own forbears is made obscure by the scandalous fact that there is not a single biography of Say in the English language, and precious little even in French.

Perhaps we can understand this development given the following. In France, economics had long been associated with the physiocrats, *les économistes*. The ouster from the controller-generalship of the great Turgot in 1776 and the consequent demise of his liberal reforms served to discredit the entire physiocratic movement. For Turgot was unfortunately considered in the public eye as merely a fellow-traveller of physiocracy and its most influential follower in government. After this loss of political influence, the French *philosophes* and the leading intelligentsia felt free to heap mockery and ridicule upon the physiocrats. Some of the fanatical cult aspects of physiocracy left it vulnerable to scorn, and the *encyclopedistes*, though themselves generally pro-*laissez-faire*, led the attack.

The advent of the French Revolution accelerated the demise of physiocracy. In the first place, the Revolution was itself too intensely political to allow much sustained interest in economic theory. Second, the physiocrats’ strategic devotion to absolute monarchy tended to discredit them in an era when the monarch had been toppled and destroyed. Moreover, the physiocrats,