



Constitutional Implications of Radical Subjectivism

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Abstract. This paper examines the role that creative choice, as stressed by Shackle, plays in the generation of economic value. In particular, we evaluate the relationships between creative choice, economic value and the institutional structure of an economy.

Key Words: constitutionalism, creative choice, entrepreneurship, subjectivism

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1. Introduction

In an earlier paper, we examined the apparent affinities between the radical subjectivist research program in economic theory and those programs in the physical sciences that analyze patterns of order in away-from-equilibrium settings (Buchanan and Vanberg 1991). If single names are helpful, our earlier paper could be summarized as an effort to compare the approach to economic theory associated with the work of G.L.S. Shackle with the approach to physics associated with the work of Ilya Prigogine and his followers. In this follow-on paper, we propose to examine more carefully the role that creative choice, as stressed by Shackle, plays in the generation of economic value. In particular, we want to evaluate the relationships between creative choice, economic value and the institutional structure of an economy.

We shall suggest that a generalized failure to appreciate the role of creative choice in providing the dynamic for economic interaction may have been an important causal element in economists' failure to escape from the "fatal conceit" that socialist organization represented (Hayek 1988). To put our central conclusion dramatically, but succinctly, we shall argue that socialism failed not only because of incentive incompatibility and an inability to utilize knowledge effectively; socialism failed, also, because it allowed little scope for the exercise of creative choice on the part of the participants in the economic process. Or, to state the conclusion somewhat differently, universalized benevolence could surmount the incentive incompatibility; universalized omniscience (in its usual meaning) could surmount knowledge limits. But even perfect altruists who know everything must live and work in real time. The best of intent will not allow the future to be brought within the present, no matter how perfect the knowledge of the present may be. And if the institutional structure embodies the presupposition that such a feat is possible, stagnation and failure must emerge.

In Section 2, we return to basics, and we define *creative choice* by comparison and contrast with that which one of us has called *reactive choice*, almost the exclusive domain of orthodox economic analysis (Buchanan 1989). And we relate this two-part classification of choice to two strands of interpretation of the entrepreneurial role in a functioning market

economy. This classification of the entrepreneurship role may, in turn, be related to the presumed exogeneity or endogeneity of the sources of economic value. In Section 3 we apply the analysis to the question of organizational-institutional structure, contrasting market process and socialist economy. We suggest that claims for the potential efficacy of socialist economies must have incorporated neoclassical presuppositions that ignore the role of creative choice. We suggest that no one who is informed by Shackle's vision of economic process could possibly have expected socialism to work effectively. In Sections 4 and 5 we discuss some implications of radical subjectivism for constitutional analysis and the role for constitutional choice. Section 6 concludes the paper.

2. Creative Choice in Economic Process

In the textbook paradigm of neoclassical microeconomics, there exists (1) a set of preference or utility functions that fully describes the internal evaluations of all participants in the economy, the trade-offs among the potential goods and services that might be produced; (2) a set of resource endowments that is capable of being employed to produce the goods and services that are positively valued and (3) a set of available technologies that provides complete instructions as to how resources can be transformed into valued goods. In this setting, "the economic problem" (Robbins 1932) becomes that of allocating scarce resources among uses so as to achieve a maximum of economic value. Any shortfall from this maximum involves a wastage of value potential, and any move toward eliminating such wastage amounts to an increase in realized value. But there is no creation of *new* value potential in the model. The idealized competitive market works so as to "squeeze out" all of the value potential that is ultimately defined by the coexistence of preferences, endowments and technology. The imagined allocative exercise of the organized market order in this stationary setting is categorically separated from the operations of this order that may modify the structural parameters, those operations that may shift the preferences, endowments or technology of the economy. And, as we know, there is no explanatory paradigm for this second level of operation that is even remotely comparable in scientific acceptability or aesthetic beauty to the idealized market's maximization of economic value.

What happens as the idealized market organization operates so as to squeeze out the full value potential? Presumably, the participants in the economy, in their varying roles, choose *reactively* to exogenously generated changes in one or more of the parameters of the system. A change in rainfall patterns will, for example, modify the resource base and will affect the allocation that will maximize value in the economy. That pattern of resource usage in existence prior to the climatic change will not satisfy the conditions of value maximization after the change. And individuals, in their capacities as resources owners, entrepreneurs and consumers will respond to the apparent disequilibrium in separated markets that reflect the changed parametric setting.

The neoclassical parable need not be elaborated further here. We stress only a single feature for the whole exercise. Participants are modelled as responding to exogenously generated shifts in the parameters of the economy. There is no place in the model for choices and accompanying actions that *create*—rather than exhaust—economic value, choices and actions that are endogenous to the operation of the market process itself.

The absence of creative choice in the neoclassical model has not gone unnoticed, even apart from the fundamental challenge raised by Shackle and his followers. Especially because of the implied relegation of entrepreneurial choice to a reactive role, effective criticism of the neoclassical model has been advanced by economists who claim affinity to seminal Austrian sources, notably by Schumpeter (1934) and Kirzner (1973), who develop differing analytical frameworks. In the Schumpeterian model of economic process, the activity of entrepreneurs brings value into being that did not exist as some dormant possibility prior to such activity. In the absence of the activity of the entrepreneur, there is no increase in value potential. The theory of entrepreneurship developed by Israel Kirzner remains closer to the neoclassical orthodoxy, but his analysis may also be interpreted in such a fashion as to allow entrepreneurial profit to be considered endogenous.

Shackles's criticism is, of course, much more far-reaching than the Austrian, and it does not single out the entrepreneur for special analysis and examination. Shackle's central focus is on the elementary fact that choice, any choice, occurs in real time, and that the act of choice itself creates a future that does not exist independent of the choice that is made. As one of us has suggested elsewhere, Shackle may have generalized his insight too readily to all choices (Buchanan 1989). Many actors in the economy choose only in response or reaction to creative choices made by others with whom they may interact. That is to say, the neoclassical world may be descriptive of the behavior of many market participants. For such participants, the choices made do indeed create the future that they experience, but, within limits, the patterns of choices may be predicted from the shifts in the parameters. There remain, nonetheless, participants in economic process who may choose and act creatively in a sense analogous to Schumpeter's entrepreneur. And importantly for our purposes here, any participant in the process may, if he or she so wills, act creatively rather than reactively.

If we acknowledge that choice may be creative rather than reactive, and that at least some actors in the economic process can be expected to act creatively if given the opportunity, it becomes clear that the presuppositions of the neoclassical paradigm are misleading. The postulated fixity of preferences, endowments and technology must be violated for creative choice to occur at all, and, as it does occur, there is no maximum of potential value to be secured in an equilibrating process. The potential value frontier is continually being pushed outward by the creative choices of some participants, who by their actions are continually modifying the parameters to which reactive participants must respond. The whole notion of a value maximum attainable from "the economy," as such, had best be abandoned, lest one wants to claim that man's creativity is exhaustible.

3. Creative Choice, Markets and Central Planning

As we noted in our earlier paper, the distinction emphasized is that between a teleological and a nonteleological interpretation and understanding of market process, and, by extension, of the institutional-organizational structure that constrains the behavior of participants in such process. The neoclassical definition of "the economic problem" to be resolved, the allocation of scarce resources among alternative end uses, more or less directly points toward a maximization exercise, which, in turn, implies the independent existence of a maximand, a scalar against which efforts at resolution may be evaluated. From this perspective

the performance-test for institutional-organizational arrangements is that of comparative “efficiency” as measured in value units that exist as potential-to-be-realized in the initial configuration of resource and technological capacities. The institutions of “the market,” that is, private property and voluntary contract enforceable under law, describe *one* alternative means or “mechanism”; the institutions of socialist central direction describe another. Which arrangement delivers value more effectively? The test is conceptually straightforward.

Yet, if choices made and actions taken involve more the exploitation of the potential value that already exists, if new potential value can be brought into being by the behavior of participants, it follows that a value scalar that is independent of choice cannot exist. The whole utility maximizing logic for “explaining” choice can be rescued only if it is emptied of operational content by defining “that which is maximized” as “that which is chosen.” The institutional-organizational comparisons that seem straightforward in the standard neoclassical enterprise cannot be made. There is no scalar against which comparative results may be assessed. If economic value is not separate from that pattern of results which emerges from choices made and actions taken by individual participants in the process, differing organizational parameters will generate incomparable patterns of results. At such a level, nothing more can be said.

The basis for any normative or evaluative judgment must be shifted from patterns of results to characteristic features of the institutional-structural parameters themselves. And we recognize that these features are dramatically different in the market economy on the one hand and the planned or socialist economy on the other. If we restrict attention to “pure” models, we may isolate and identify the liberty of entry and exit into and out of occupational, locational, institutional and behavioral categories as central to market order. Persons may, voluntarily and individually, choose among separate professions and occupations; they may choose where to live and to work; they may choose among many sources for employment, including self-employment; they may choose among rates of input supply; they may choose among separate bundles of commodities for final usage. This freedom of choice that is the characteristic feature of market organization has no direct relationship to the results of the choices that are severally made by all of the participants.

The centrally planned or socialist model for the workings of an economy is, by contrast, purposefully related to a predicted pattern of results. The very notion of planning must presume some well-defined end objective of the plan itself. It is evident that the idea of a planned economy is inconsistent with the idea of voluntary choice on the part of participants in the economy. If a plan is to work, participants must act in accordance with the dictates of the plan, even if, in some ultimate sense, these dictates are themselves determined by preferences of individuals (as, for example, in pure market socialism). Our concern here is not at all with whether or not, and to what extent, a planned economy might be successful in achieving that pattern of results that is sought. Our emphasis is on the basic incompatibility between any planning model of economic process and the exercise of genuinely creative choice on the part of participants anywhere in the inclusive economic nexus.

Recognition of the categorically different “space” allowed for the exercise and implementation of creative choice in the market and the planning model for economic organization prompts a prediction of the relative failure of efforts at economic planning on the part of anyone who assigns creative choice a central role in the dynamics of economic process. G.L.S.

Shackle should have, necessarily, and from the very logic of his methodological position, understood that the whole socialist experiment was an exercise in folly. And Shackle, or any Shacklean, could have come to this stance independent of any prediction or evaluation of comparative results based possibly on differential utilization of knowledge as between the market and the plan or even on the differential incentive compatibility in the two settings.

In what follows we shall discuss in more detail some of the general conclusions that a recognition of the role of creative choice suggests, not only for a comparison between the two above institutional-organizational alternatives, but for the general issue of institutional-constitutional choice. More specifically, we shall examine, from a contractarian-constitutional perspective, the kinds of arguments that become relevant in matters of constitutional choice, if one takes the role of creative choice into account.

4. Constitutional Framework and Creative Choice

It is useful, for the task at hand, to conceptualize all human activity—whether separately or collectively organized, private or public—as *problem-solving behavior*. With such conceptualization the issue of *creative choice* can be specified as the question of how new, and potentially better, problems-solutions are to be tried out and to become adopted. And to inquire into the constitutional implications of radical subjectivism means to examine the question of what constitutional rules we may want to live under, if we take into account the role of human creativity.

The concept of problem-solving behavior immediately invokes the related notions of problem-solving capacity and problem-solving knowledge, making apparent that the issue of creative choice is, essentially, about the role of *knowledge* in the creation of economic value. The growth of (problem-solving) knowledge and the creation of economic value are inherently tied to each other, and to find a constitutional framework that is conducive to the former, is to find one that enhances the latter. It must be a framework that provides room for human creativity and innovativeness, a framework in which individuals—separately or collectively—can explore and find new and better solutions to “old” problems, as well as discover and try out solutions to “new” problems.

When we conceptualize human behavior in all its varieties as problem-solving efforts, two simple insights command attention.

The first is that we cannot know today what we shall know tomorrow and that, therefore, we cannot know in advance what the “best” solutions to our problems may be. Human problem-solving behavior is an ongoing, continuous and open-ended process in which constantly new knowledge is created. At no point can we know which new solutions to our problems may be discovered tomorrow. We will, of course, based on our current knowledge, seek to identify the “best” solution available. But, we cannot know what creative minds may invent tomorrow or, for that matter, even in the next minute. As Shackle (1983:37) has phrased it: “The bounds of the possible are bounds of unknowledge.”

The second insight is that we cannot know what problems we may face, or what we shall perceive as our problems, tomorrow. To be sure, this does not mean that we cannot have informed expectations about the future, nor does it mean that we should not try to anticipate, as well as possible, problems that lie ahead. Yet, our problems of tomorrow are,

ultimately, as unpredictable as our knowledge of tomorrow, in part as a consequence of the latter. Solutions that we find for our current problems are likely to create new problems, problems for which we then, again, have to find solutions. And any attempt to halt this process cannot be anything but futile.

The above line of argument is clearly in the spirit of Shackle's emphasis on the unknowability of the future. Yet, it should be noted that such view does not imply an attitude of passive acquiescence with whatever emerges. As Shackle has argued, an adequate understanding of the role of human choice has to find its place between two extremes on the one side, a deterministic view for which human choice does not matter because the future is already completely predicated in the present and, on the other side, a view for which choice "can make no difference" because "each present leaves its successor wholly unconstrained, so that any state of the world can be followed by any other state" (Shackle 1979:20).¹ While radical subjectivism undermines the enterprise of forecasting particular future states, it does not deny the role of what Hayek has referred to as "explanations of the principle" or "pattern predictions" in our efforts to provide for the future. In particular, it does not deny the role of efforts to shape the institutional-constitutional arrangements under which we live. Unknowability of the future in a Shacklean sense does not mean that we cannot understand the general working properties of rules and institutions, and that such understanding can inform our choices among alternative constitutional regimes.

To acknowledge the role of human creativity, of inventiveness in coming up with new problems-solutions and, at the same time, to see a role for constitutional choice and institutional design, clearly points out the general direction into which such efforts must go, namely the creation of a framework for creative exploration at all levels of problem solving. Where we cannot know in advance what solutions to our problems may be found, and what the best solution may be, but where we can identify the general criteria against which to measure the "goodness" of solutions, we can seek to set up a framework for a competitive process of evolutionary learning, a framework that allows for diversity and innovation, but subjects the experimental exploration to a selection process that selects in favor of solutions that we consider desirable.

That is, we shall not only be interested in a constitutional framework that provides room for innovativeness and experimenting with new solutions, we will also be interested in a framework that *constrains* the process of exploration so as to assure its responsiveness to our, the constituents,' interests. Such constraints come, in the first instance, in the form of general rules that limit what the participants in the process may lawfully do, typically by excluding certain kinds of actions or strategies from the permissible set. And they are embodied in the mechanism of selection that sort out the experimental trials into successes and failures.

The three above features—the freedom to experiment with alternative solutions, constraining general rules and a selection-mechanism²—appear to be essential ingredients of any constitutional framework for human creativity, a framework for learning by trial and error, for evolutionary adaptation. The nature and the interaction of these components will determine whether, and to what extent, the process that they condition will be responsive to the interests of the persons involved. In the absence of the freedom to experiment and to innovate, stagnation must result. In the absence of suitable rules-constraints, the process may systematically produce outcomes that are undesirable to its constituents. And the same

is to be expected in the absence of an appropriate selection mechanism, “appropriate” in terms, again, of the interests of the persons involved, the constituents.

Markets are an obvious paradigm example of a constitutional framework with the above characteristics, and it is instructive for our purpose here to examine briefly their respective properties.

5. Constitutionally Constrained Evolution

It has often been noted that the market process exemplifies an *evolutionary* process. What we want to emphasize here is that markets are a paradigm case of *constitutionally constrained evolution*. They provide not only room for trying out and exploring alternative solutions to problems, they are embedded in a constitutional framework that is supposed to make the explorative process work in ways that serve the interests of the participants.

The constitutional framework delimits, first of all, the domain of markets, that is, it defines the range of problems for which solutions can be explored in market competition, as opposed to those problems that are assigned to the public domain. Within their respective domains, evolutionary market processes operate under the constraints of rules that limit what participants may lawfully do. And they are subject to a selection mechanism that makes for responsiveness to consumers’ interests, that is, to the interests of the “sovereigns” who are the ultimate judges over success and failure.

Markets not only allow for experimenting with alternative solutions to a broad range of problems, they encourage exploration and provide incentives for the discovery of new solutions. That is, they promote the growth of problem-solving knowledge. Hayek’s classical argument on the “use of knowledge in society” seems to be mostly remembered for its claim that the capacity for utilizing dispersed knowledge makes markets superior to central planning. Yet, there is a second part to Hayek’s argument that is closer to our present theme, namely the role of competition as a *discovery procedure*. The recognition of the role of creative choice in the generation of economic value points to a knowledge problem that goes beyond the problem of utilizing existing knowledge, namely the growth of knowledge over time. It is in this regard that the market’s dynamic properties “as a process of exploration” (Hayek 1978:188) come into focus. While central planning already stumbles over the “dispersed knowledge” problem, concentrating on the market’s capacity to utilize such knowledge underestimates its true knowledge potential. Markets do more than utilize existing knowledge, they encourage and promote innovative exploration and the creation of new knowledge. They provide a framework for what Hayek³ has aptly called an “exploration into the unknown.”

The extent to which markets do, in fact, serve the interests of those who do the ultimate “selecting,” the consumers-sovereigns, is, of course, dependent on the nature of the constitutional framework that conditions their operation. The question can, therefore, be raised whether this framework itself—i.e., the definition of the domain and the rules under which markets operate—is desirable, “desirable” in terms of the interest of the members of the respective community or, in other words, of the relevant citizens-sovereigns. This question concerns the comparison among alternative constitutions, a comparison that can only be

made at the constitutional level itself, not at the sub-constitutional level of within-market operations.

At this level, the knowledge problem reemerges again. To establish an appropriate constitutional framework for market processes—where “appropriate” is to be defined in terms of the interests of the relevant group of constituents—is itself a problem for which we cannot claim to know the best answer in advance and forever. Acknowledging our limits of knowledge at this level can certainly not mean that we should abstain from deliberate constitutional construction. But it suggests that we should provide for a (meta-)framework in which there is room for alternatives to be explored, and in which selection mechanisms are at work that make for responsiveness to the interests of the relevant constituents.

The concept of *constitutionally constrained evolution* implies that the notions of constitutional choice and evolution are not as far apart as they are sometimes perceived. To acknowledge that we can never know in advance what the best solutions to our various problems may be, nor what problems the future may bring, is not an argument against deliberate problem-solving efforts. It is, however, an argument for allowing our problems-solutions to be challenged by alternatives, for utilizing the explorative potential of an evolutionary process in which new solutions can be tried out. To realize that we cannot expect evolutionary forces “per se”—i.e., in the absence of appropriate constitutional constraints—to bring about what we find desirable, means that we ought to seek to create a constitutional framework that can be expected to make the explorative-evolutionary process responsive to our interests. For these constitutional constructions we need, again, to recognize that we face a knowledge problem that requires us to allow for the exploration of alternatives. And this interaction of evolution and design applies to all levels at which we seek—separately or collectively—to find solutions to the problems that we face, including the level at which we choose the most inclusive rules within which all our other efforts in problem solving take place.

Furthermore, evolution and constitutional choice are interrelated in the sense that all our constitutional constructions are for units that themselves are embedded in a wider environment where they are exposed to forces of evolutionary competition. If we use the term *constitutional system* for a social unit that is defined by a common constitution, we can think of the social world as a complex arrangement of interlocking constitutional systems (e.g., a firm in a local market that, again, is embedded in a larger market and a polity, the latter, again, being embedded in a more inclusive constitutional environment, and so on), each of which faces the problem of finding a constitution that, internally, has the working properties which are desirable to its constituents, while, at the same time, allowing the system to be viable in its larger environment. Therefore, our constitutional choices for any particular unit are constrained by the competitive forces to which it is exposed in its own environment. Not all constitutional regimes that we may find desirable for other reasons need to be viable in this sense.

6. Conclusion

If there is one central constitutional implication of radical subjectivism, it is the recognition that a constitutional framework which accounts for the creativity of the human mind has to be one that allows for, and provides, favorable conditions for learning and adaptation at

all levels at which we engage in problem solving, including the level at which we choose the constitutional framework for all other efforts. It should be a framework within which experimenting and exploration are possible, yet one that imposes constraints on the explorative process that make for responsiveness to constituents' interests as well as for viability in a broader environment. Markets are, as we have suggested above, a paradigm case for such a framework, and the constitutional implications of radical subjectivism may also be stated in the form of a recommendation that we ought to seek, in general, at all levels of problem-solving activity, to provide for market-like frameworks⁴ for competitive exploration of alternative solutions. To recommend, in this sense, the market as a model for explorative, adaptive systems, is not to say that we ought to leave everything to "the market," in the ordinary sense. It is to say that we ought to expose our solutions to the various problems we face to competitive constraints that work like market constraints.

Notes

1. Shackle (1979:20): "The anarchy of Nature is as fatal as the determinacy of Nature to the notion of choice as a source of history."
2. The selection mechanism can also be viewed as an aspect of, or an implication of, the relevant set of constraining rules. We find it useful here to mention it as a separate item.
3. Hayek (1948:101): "The solution of the economic problem of society is in this respect always a voyage of exploration into the unknown, an attempt to discover new ways of doing things better than they have been done before. This must always remain so as long as there are any economic problems to be solved at all, because all economic problems are created by unforeseen changes which require adaptation."
4. As Wiseman (1989:277) has noted about the appropriate attitude in a world in which the future is unknowable: "For such a world we have established one ineluctable rule of social efficiency: that there should exist no rule that does not incorporate an acceptable procedure (rule) for its own change. This derives from the unknowability of the future, which in turn predicates the likelihood of mistake, as much in the context of decisions about governments and institutions as in decisions about market behavior."

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