

## **A Practical Approach to Understanding: The Possibilities and Limitations of Applied Work in Political Economy\***

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**Abstract:** What can the applied economist do? In order to explore issues playing out in the ‘real world’ of the past or present, the applied social scientist has to make a series of decisions about what they will accept as the facts of the situation. Particularly for research questions in which the beliefs, plans, and motivations of individuals matter—such as institutional analysis—this task requires the development of some degree of intersubjective understanding, or *verstehen*. For over fifty years, the Bloomington School of Institutional Analysis has been using fieldwork and deep archival history to conduct meaningful institutional analysis that takes interpretation and the quest for understanding seriously. As such, those who wish to take up the call for economists to take an “interpretive turn” can gain a great deal of insight and practical advice from the study of the Bloomington School’s methods and approach.

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“...while it is easy to show the absurdity of most concrete attempts to make the social sciences "scientific," it is much less easy to put up a convincing defense of our own methods...”  
--F. A. Hayek (1943, p. 2)

## **I. Introduction**

In order to explore issues playing out in the ‘real world’ of the past or present, the applied social scientist has to make a series of decisions about what they will accept as the facts of the situation. This task is a difficult one because observed action is but an imperfect window through which to study human behavior. Even aside from the possibility of deliberate misrepresentation, which is itself a significant issue, particularly in political economy, there is room for a range of interpretations in how the facts of a situation are perceived, communicated, and recorded.

The difficulty of characterizing the simple facts of the situation in order to be able to subject them to explanation by economic analysis is exacerbated by the subjective nature of the facts of the social sciences. There is a very real sense in which the tools and objects of the social world are not meaningfully definable by objective characteristics, but only by “what people think they are” (Hayek 1943, p. 3). A hammer is just an oddly shaped bit of wood and steel unless one possesses a belief about its value in use. This is a direct implication of thinking about economics as the study of purposive behavior. If the phenomenon of interest is the development and actualization of plans by individuals in the social world, then the nature of the plans individuals make is an integral part of the science of human action. And, lacking access to some record of objective truth that can be referred to in cases of uncertainty, individuals have no alternative but to create these plans based on their own beliefs about relationships between cause and effect.

The interpretive ambiguity generated by the subjective nature of the social world, has the potential to create real problems for the conduct of any sort of applied research (Lavoie 1990a). If individual’s values are determined subjectively, and if individuals choose based on

subjectively defined expectations, then observed action is only one of many layers necessary for the empirical study of human behavior. Any given action could potentially be consistent with any number of social motivations and strategies. As such, limiting empirical work in the social sciences to the mere copying down or quantification of observed choices and outcomes puts severe—and, we argue in this chapter, unnecessary—limits on the potential for applied work in the social sciences. This is especially true for institutional analysis. Understanding the beliefs, plans, and motivations of individuals is critical to understanding the form and function of the rules and constraints that combine to form economic, social, and political institutions. As such, when institutional analysis is broadly defined as any system of rules shaping human behavior, this means that there are few, if any, areas of social inquiry that would emerge unscathed from a prohibition on the discussion of subjectively defined beliefs and expectations.

Consequently, applied work requires the development of some degree of intersubjective understanding, or *verstehen*. The version of the concept of *verstehen* we use in this paper is that developed by Max Weber and then adapted into the discipline of economics—sometimes explicitly, sometimes implicitly—by Ludwig von Mises, F. A. Hayek, Ludwig Lachmann, and other thinkers in the Austrian tradition (Boettke and Storr 2002, Hayek 1943, Lachmann 1971, Weber [1922] 1968). The core of the idea is that the understanding of events in particular times and places—in other words, applied research—cannot proceed on either the context-less accumulation of isolated observations or pure deductive logic alone. Instead, theory and the facts of human experience are connected through a process of historical interpretation that allows the observer to make sense of a historical episode. Intersubjective understanding is a requisite component to both action in the social world and to attempts to theorize about the social world.

What it means to understand in an intersubjective way and how intersubjective understanding is acquired will be considered in the third and fourth sections of this essay.

The final claim to be made in this essay is that meaningful institutional analysis that takes Austrian concerns about the subjective nature of the facts of the social sciences seriously is a significant component of the work of the Bloomington School of Institutional Analysis (hereafter, Bloomington School). In their decades of research on common pool resources, local public goods, and the development of systems of self-governance, Elinor and Vincent Ostrom and their colleagues used methods explicitly designed to develop intersubjective understanding. In particular, the fieldwork and deep archival history conducted by the scholars of the Bloomington School enables the social scientist to enter their subject's social world in a way that ameliorates some—though not all—of the limitations associated with studying subjectively constituted individuals in complex systems. Those doing applied work in Austrian economics who wish to take up the call issued by Don Lavoie (1994) for our discipline to take an “interpretive turn” into the serious study of subjectively defined meaning and beliefs can gain a great deal of insight and practical advice from the study of the Bloomington School's methods and approach.

This essay begins with an overview of the relationship between theoretical and historical study in the Austrian tradition which demonstrates the need for an analytical link that allows the researcher to gain access to the meaning subjects ascribe to their actions, whether that link is labeled *verstehen*, or interpretation, or intersubjective understanding. In section III, we explore the concept of intersubjective understanding in greater depth, including its implications for choice of method when conducting applied research. Section IV demonstrates the use and value of methods that prioritize intersubjective understanding by drawing on research conducted by

scholars in the Bloomington School of Institutional analysis. Section V concludes with implications and a discussion of what contemporary Austrian economists can hope to meaningfully borrow from their colleagues in Bloomington.

## **II. Theory and History**

Mises defined praxeology as the science of human action: a body of general theory “valid for every human action without regard to its underlying motives, causes, and goals” (Mises 2007 [1949], p. 21). This body of theory is derived from a simple set of postulates about the nature of human behavior. Specifically, that people are capable of imagining states of the world in which they are better off; that this gap between where they are and where they could be is experienced as a source of uneasiness; and that when they come to believe that a particular action will remove some of that uneasiness, they will act. This is not a significantly different formulation than the economic theory found in the opening chapters of most introductory economics textbooks, which teach that people are sufficiently rational to identify and act upon profit opportunities, i.e. ways to make themselves better off. As such, his analysis of the relationship between theory and history is relevant for a variety of styles of economic theorizing.

Theory is a powerful tool, but on its own it can do little to help us better understand the world we live in. Most of us find it difficult to even contemplate theory without either direct or indirect reference to the world of human experience. This is why a familiar example can be so useful in conversation about even relatively simply abstract principles. Consequently, history, defined as “the collection and systematic arrangement all the data of experience concerning human action” is the irreplaceable counterpart to theoretical inquiry into human choice (Mises 2007 [1949], p. 30). As explained by Lavoie (2011, p. 116-122), the characterization of Mises as

wanting to maintain strict separation between theory and history is a misinterpretation of his views. Rather, as the applied nature of most of his own work suggests, he saw theory and history as being distinct but also both absolutely necessary for any real understanding of human society.

There are (at least) two reasons why the historical component of the applied researcher's task is so difficult. One of these sources of difficulty is that there is simply too much information to be able to collect and arrange *all* of the data of human experience into a complete record. The researcher instead prioritizes, selecting only the most relevant facts according to their theories about which factors in the social world can potentially have an important causal impact on an individual's choices and actions (Mises 2007 [1949], p. 47). This is by no means a defense of cherry-picking the bits of information that will be most useful in proving a particular theory. Every researcher, even those who strive for and attain the highest possible level of value-freedom, must select a set of theories they judge to be worthy of scientific investigation and then proceed with the selection of articulable bits of information that will speak to the validity of those theories. What results is a historical record that is a representation of history, not a perfect reproduction (Mises 2007 [1949], 46-64).

The second reason why the 'applied' part of applied research is so difficult is that in the social sciences, "what matters is not things themselves, but what things mean to people" (Lavoie 1991, p. 470). People make choices based on their own subjectively determined valuations of the alternatives available to them. The objective realities of the physical sciences are important for determining the results that will occur in response to an individual's choices, but they do not determine the choice itself. Instead, it is the subjectively held beliefs of individuals that shape their expectations about the value and likely results of particular courses of action, this shaping their behavior in the most meaningful ways (Hayek 1943, Lachmann 1978 [1956], Lewis 2008).

In other words, the beliefs that an individual holds about the world outside themselves is the mechanism through which the external world has a causal impact on human choice. This view—that the value people attach to particular outcomes and courses of action is determined subjectively and in the moment—is so integral to the Austrian tradition in economics that it is considered the traditions’ most important defining characteristic (Lavoie 1990b, p. 363; Lavoie 1991).

The Austrian notion of subjectivism problematizes applied research because it calls attention to the fact that one of the most important determinants of individuals’ choices—their subjectively held beliefs—is in a sense unknowable. Except for the instant within which an action takes place, at which time you may get an imperfect window into what an individual intended, assuming there isn’t too much interference with the signal, there is no way to be sure as an outside observer that you have correctly intuited an individual’s values, motivations, or intentions.

One possible solution to this problem is to simply substitute an understanding of the individual’s subjective preferences for the researcher’s own subjective preferences, or for an ‘objective’ external conception of what their preferences are presumed to be. This is easy enough to do—after all, the researcher already has access to their own beliefs, and if some idealized set of preferences is to be devised, the possibilities are near endless. However, this is a scientific move that is incompatible with a social science that views people as autonomous agents and attempts to understand them as they truly are. The Austrian critique of the new paternalism illustrates the pitfalls that accompany an approach that ignores considerations of subjectivity (Rizzo and Whitman 2008).

Another possible solution is to ask the individual why they made a particular choice, or what choice they would make if they were to act. This is obviously problematic when compiling information related to people who are no longer living or otherwise inaccessible, but even in the absence of these formidable constraints, asking someone directly about their preferences does not guarantee you will get good information. There are many reasons why an individual may want to lie about their true preference orderings (Mises 2005 [1957], p. 13). For instance, a woman with a sweet tooth may say she doesn't care for cake, even if she would quickly polish off a slice were it set in front of her. There are a multitude of possible reasons for even this relatively trivial falsehood, all of which have different implications for her underlying preferences and motivations. She might lie strategically, to get a free sample from a bake shop, or as part of a campaign to convince someone else to give up their own treat. If she's trying to cut back on sweets, she might lie as a pre-commitment device to raise the social cost of future cake consumption, or to cultivate an image of herself as a more restrained person. She might lie as a social grace, to encourage someone else to feel more comfortable about eating the last slice from the pan.

There are a number of important insights illustrated by this simple scenario. First, it illustrates the limits on the knowledge that can be gained even if we are able to observe the individual at the moment of choice. As observers watching a woman refuse a slice of cake, all we can know is that some other object was more valuable to her in that moment. We cannot know why she made the choice, or what that other more valuable object might have been. We certainly cannot use that moment of choice to discern between different possible motivations. Further, even if we asked the woman about her choice directly and she attempted to honestly communicate her values and preferences, she might not succeed. The use of language to

communicate ideas to a second (or third) party is fraught with the possibility of misunderstanding.<sup>1</sup>

Depending on why we are interested in observing this particular choice, we may or may not care about understanding the woman's motivations. There are many questions that her intentions are irrelevant to answering—how much cake is left, how many people got a slice, etc. But there are many more questions that do require some degree of intersubjective understanding to be able to address. At this point we can abstract away from cake, the stakes of which are relatively low, and broaden the focus of the question. Say we're talking about an individual deciding whether or not to buy a newly developed product, or to sign up for a welfare benefit, or to participate in a cooperative rule-making organization, like a neighborhood association, water board, or local government. *Why* she might or might not opt in to these things matters. It matters to the entrepreneurs, politicians, and neighbors who are making choices based on their expectations of how she is likely to behave in the future. And because it matters to the individuals who are making choices, it also matters to social scientists interested in exploring patterns of cooperation, and how it is that people can come to peaceable agreement based on mutually compatible sets of expectations.

The difficulty of interpreting the meaning behind human action is one reason why economists are often advised to stick with analysis that doesn't inquire into motivations, but instead proceed in as value-free a manner as possible with the evaluation of the suitability of alternative means to the attainment of a particular end. Some may even fear that really dealing

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<sup>1</sup> Don Lavoie (1990a, p. 177) pushes this point even further by suggesting that the only way to fully understand a situation as the acting individual perceives it is to *replace* our perspective with their own. This full immersion in another person's perspective would defeat the purpose of the attempt to understand entirely; instead of one individual interpreting the actions of another, the researcher would be back where he started, with the understanding of a single perspective.

with subjectivity is analytically squishy enough that it could deprive social scientists' of their rigor and their access to insight (Lavoie 1990, p. 170). However, the world we live in is inescapably constituted by people interacting with each other based on subjectively held beliefs. Even when these beliefs and expectations are flawed, they still shape what actions people will take and therefore the observed results of exchange behavior, such as prices and patterns of production (Lachmann 1990). Consequently, subjectively defined expectations often have a greater impact on action and therefore observed patterns of human behavior than the fixed external constraints that are often seen by economists to be the primary determinants of choice.

These complications mean that the task of interpreting and organizing the subjective data of human experience so that it can be rendered intelligible by economic reasoning is a serious project worthy of consideration in itself. Don Lavoie defined this project as *hermeneutics*, the study of “the way in which, in the sciences, the arts, history and everyday life, we manage to come to an understanding of other people’s actions and words” (Lavoie 1990a; Lavoie 1990b; Lavoie 1994, p. 55).<sup>2</sup> Implicit within this approach is the judgement that the scientific characterization of a subject can be so different from the reality that theoretical inquiry will no longer be relevant to the real world phenomenon, but only to the fictionalized characterization created by the analyst. When this happens, the social scientist is no longer engaged in a project designed to render the social world more intelligible; instead, the analyst and theory are primary while the subject of the inquiry recedes into the background.

Ultimately, the answer Lachmann provides as to why it is valuable to pursue intersubjective understanding through a hermeneutical approach is that social scientists need “conceptual schemes more congenial to the freedom of our wills and the requirements of a

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<sup>2</sup> I will not re-state here the conversation about hermeneutics that has taken place in the economics literature. For a more thorough summary, see Storr (2010).

voluntaristic theory of action than anything we have at present” (Lachmann 1990, p. 137). In the remainder of this paper, we will first define this project and its relevance to both the Bloomington and Austrian schools of political economy, and then illustrate the use value of the methods developed by the Bloomington School for dealing with problems of interpretation and the intersubjective nature of social science.

### **III. The Problem of Understanding**

The concept of understanding, or *verstehen*, is a bridge intended to connect the deductive reasoning of economic logic with particular historical applications. In *Human Action*, Mises defines it broadly, as “the elucidation of the unique and individual features of the case” through “the mental grasp of phenomena which cannot be totally elucidated by logic, mathematics, praxeology, and the natural sciences” (Mises 2007 [1949], p. 51, 50). In so doing, Mises is drawing on the Weberian tradition of seeking to understand the subjectively defined meanings that shape the choices individuals make in the process of purposive action (Boettke and Storr 2002). Although many definitions of *verstehen* have been proposed at various times and in various disciplines, the common thread seems to be that it is a kind of cognition that occurs separate from scientific reasoning that enables us to ascribe some degree of meaning to the actions of our fellow human beings (Maki 1990; Mises 2007 [1949]; Selgin 1988). As such, in this paper, we consider *verstehen*, historical interpretation, and intersubjective understanding to be equivalent concepts.

The importance of intersubjective understanding is perhaps best illustrated by Kirzner’s (1976) example of a Martian looking out over Grand Central Station. The Martian notices bodies of a variety of shapes and sizes, covered in a variety of different styles of ornament, boarding

metal boxes headed in a variety of directions. Over time, he notices that the station is busier in the mornings around 8:00, and in the evenings around 5:00, except for two out of seven days, which seem to have a lighter and less variable traffic pattern. If he were well-versed in statistics he could formally model this behavior. But lacking the understanding of human experience, this Martian observer may struggle to identify the meaningful commonality that drives the behavior of all these diverse actors: the fact that they are commuters, going to work at a similar time every weekday morning, and heading home again at a similar time every weekday evening.

What exactly is it that gives the citizen of Earth an advantage over the Martian when it comes to understanding the goings on in Grand Central Station? In *Epistemological Problems of Economics*, Mises attributed the advantage to people's ability to engage in "empathetic intuition of a whole" (Mises 1978 [1933], p. 141), though he later specifies that "Empathy and understanding are two radically different attitudes" (Mises 2007 [1949], p. 50). Don Lavoie objects to the use of the term empathy as well, because of the connotation that interpretation is a type of divination, or somehow implies that the primary goal is to be able to tell a story the way the actors involved would tell it (Lavoie 1991, p. 472; 2011). If taking subjectivity seriously requires the observer to understand the acting individual on such an intensely intimate level, then it is simply not possible to undertake empirical work from within the subjectivist tradition (Lavoie 1990a, p. 172-177).

Identifying introspection as the source of understanding is similarly fraught. Mario Rizzo (2015, p. 374-375) describes introspection as misleading because of the way in which information we receive is filtered through our own pre-existing mental constructs and classification systems. This is further complicated by the fact that our mental structures are not deliberately chosen, and as such may be unknown even to ourselves. This is always potentially

problematic for interpersonal communication, but particularly so when we attempt to process information as isolated minds without attempting to consider the mental constructs others possess by listening, reading, and watching others. Rizzo's description fits with the commonsense intuition that there is something deeply flawed with the idea of learning about others by thinking about oneself.

So, if not empathy or isolated introspection, what is it that does enable social scientists to engage in meaningful acts of interpretation? There does seem to be something quite important about the fact that much of the human experience is shared. Otherwise, what would give the Earthling an advantage over the Martian? Emily Chamlee-Wright (2011, p. 161) describes the role that being human oneself has in the study of human society as a culturally embedded individual engaging in "indwelling." In Don Lavoie's words, "There is no reason why we should not take advantage of the fact that we are already living in the phenomena we study... We need, in some sense, to get 'inside' [the agent's] perspective, in order to see how it contributed to, and was shaped by, the overall course of events" (Lavoie 1991, p. 478). Conceiving of observation in this way shifts the task of recording the data of human experience from an exercise in copying down bits of information to an exercise in something like pattern identification, wherein theory and context are used in conjunction with careful investigation to seek the best possible understanding of a situation (Lavoie 1990a; Lavoie 1990b, p. 366-372). The implication is that being able to explain the social world is not done by compiling discrete bits of information that can only be fit together in one particular way, like puzzle pieces. Instead, there are many different ways that the data of human experience can be pieced together. As such, meaningful explanation of the social world is a task that is only possible when there is sufficiently shared understanding of what the patterns of human interaction might look like.

Although presumably this is an exercise that could take place in part from ones' armchair, it is also decidedly not the cognition of an isolated mind. Instead, the culturally embedded indweller draws on their one collection of human experiences to be able to identify possible commonalities and patterns in institutions or practices that are not yet completely familiar to them. If this sounds somewhat unglamorous, that's because it is. There is nothing that privileges social scientists as having unique access to the power of understanding. Everyone uses this kind of understanding in the conduct of their daily affairs, so much so that it calls into question the possibility that an individual could ever truly act in isolation after having once lived in a society. Lavoie (2015 [1991], p. 61) gives the example of Robinson Crusoe, who even when alone on the island, still thinks in terms of a language designed for the sharing of meaning with others. Even when we are alone, we are not free of our social context, of our ability to understand and be understood.

However, even if we recognize the value of the shared human experience to the interpretive act, most are likely to find it easier to intuit the meanings ascribed to a particular action by people who have had life experiences more similar to their own. While humans share the property of goal-orientation, they vary in terms of culture, norms, and past experience. An action which would signify one thing in a society with one set of norms may signify something completely different in a separate society with a competing set of norms. The historian must situate actors within "the geographic, economic, social and historical places where they act and [in] the times in which they live" (Storr 2004, p. 18). In order to do this, the historian must have a sense of the culture, because of culture's role as "the language in which past events are interpreted, future circumstances are anticipated, and plans of action are formulated" (Lavoie 2015 [1991], p. 49). An explanation of behavior that ignores culture (or worse, assumes that the

actor's culture is the same as the historian's) ignores variables which fundamentally impact behavior (Grube and Storr 2015; Storr 2004).

The significance that social and cultural distance has in changing the nature of the task of integrating historical and empirical data into economic analysis will be familiar to even the casual historian. The greater the distance between our own tacit understandings and the tacit understandings that the subject of our investigation uses to navigate the social world, the less useful will be our own intuitions about why a particular action might make sense in a particular context. This is why Kirzner's example of the Martian in Grand Central station is so poignant. At so great a social and cultural distance as Mars, introspection is nearly useless. On a more practical scale, when working with original historical sources, it can be difficult to separate fact from fiction at the most superficial level without a sense of the stage of economic development, the social and cultural values of the people involved, their sense of humor, and the institutional context within which they were operating. This does not negate the use value of the observer's own social life, but it does mean that a light step and a deep knowledge of the historical context is required for introspection to be a useful guide rather than a hindering implantation of the observer's values into the subject's mind.

Fortunately, there are ways to cultivate intersubjective understanding. Virgil Henry Storr (2010) argues that one of the primary purposes of the debate about the relevance of hermeneutics to economic science is to argue in favor of ethnographic methods that take seriously the attempt to better understand social action. In doing so, he echoes Lavoie's claim that if economists fully understood the difficulties associated with interpreting action, then economics would "pay more serious and more "close-up" scholarly attention in its empirical research to the life-world" (Lavoie 1990a, p. 168) Emily Chamlee-Wright advocates the use of qualitative research

methods in economics, noting that methods as ethnographic field work, archival research, and in-depth case analysis “allow us to gain access to not only the actions of others, but also the mental templates shaping their action” (Chamlee-Wright 2010; Chamlee-Wright 2011, p. 166).

Qualitative methods are sometimes explicitly defined as those enabling the researcher to gain access to some degree of intersubjective understanding: “*Qualitative research* is an approach for exploring and understanding the meaning individuals or groups ascribe to a social or human problem” (Creswell 2014, p. 4). As such, the successful use of qualitative methods should enable the researcher to develop her capacity for intersubjective understanding to the extent that she remains humble, knowing that her way of viewing the world is not shared by all others, and open to the idea that people vary and that cultures do as well. The more experience that one gains in seeing how other people think, the more refined will be one’s own ability to discover the meanings that actors attach to their behavior.

Qualitative methods provide critical insights by bringing into view aspects of a problem which were previously hidden. In the case of studying the rebuilding process after Katrina, the challenge facing the researcher was not how to use a theory to evaluate all of the relevant factors at play; the challenge instead was to discover the relevant factors. This step allows researchers to refine their understanding of theory in light of what they have just learned. A theory of rebuilding efforts in the wake of disaster in which the presence of uncertainty did not play a role would be an incomplete theory. Indeed, the discovery of an important variable might be the cause for generating a theory of rebuilding. Perhaps the extent to which uncertainty plays a role is a function of other factors, including the institutional setting. If later field work in other settings found that uncertainty sometimes does not play a role in rebuilding efforts, then this finding would be relevant for theory as well. A theory of rebuilding efforts following disaster

would then ideally be able to account for the conditions under which uncertainty plays a critical role, and the conditions under which it does not. In this sense qualitative methods serve as a check on theory, and point in useful directions.

It is also worth thinking about the conditions under which it will be more, or less, important to emphasize using qualitative methods to refine our intersubjective understandings. The more important subjectively defined meaning is to being able to answer the question on the table, the more appropriate it will be to emphasize qualitative methods (Chamlee-Wright 2011, p. 161). This is particularly important for economics in the Austrian tradition that is interested in how social systems and patterns of behavior emerge as the result of an interaction between the choices of many different individuals making choices based on their own subjectively defined expectations of what it most likely to help them accomplish their own subjectively defined ends.

Before proceeding to the discussion of the methods of the Bloomington School in the next section, it is worth a brief digression to more fully address a criticism only briefly mentioned above: the concern that seeking access to the meanings others attach to their behavior is intended to imply that social scientists must limit themselves to discussing a population or event only as the people involved would have described it. Instead, the subjective meanings attached to an event by both the original actor and the observer themselves are important inputs into the interpretive process: “A hermeneutic approach demands that we recognize history not as a neutral reconstruction of the past purely on the basis of the subjective meanings of its actors, but as a mediation between a present and a past to which that present is, fortuitously, related” (Lavoie 2011, p. 111). Like the citizen of Earth is able to understand the patterns of activity taking place in Grand Central Station in a way the Martian cannot, so the historian is able to interpret the behavior of historical actors in part because of her own contemporary familiarity

with similar contexts and habits. R. J. Bernstein described these understandings that enable the historian to engage in meaningful intersubjective communication with historical actors as “enabling prejudices” (quoted in Lavoie 2011, p. 110).

Language is probably the most obvious example of the importance of intersubjective communication to being able to engage in any kind of historical or applied work (Lavoie 2011, p. 114-115). Reading is an act of interpretation in which the reader uses context and their pre-existing understanding of the social world to infer more from the text as a whole than is implied by any individual sentence or paragraph (Lachmann 1990, p. 137-138). Without access to the same linguistic concepts, it becomes remarkably difficult to infer even the most fundamental details about a historical situation. Further, when considered in historical scale, the sharing of a language is a more specific and intimate shared understanding than it may seem. Even people who do share many of the same words and linguistic traditions will encounter misunderstandings when they are from sufficiently different times and places, because of all that comes to be implied by the way in which words are used in a particular time or place. Consider, for example, how much time high school English teachers have spent explaining jokes from Shakespeare’s plays that would have been easily understood by his contemporary audience.

The ultimate implication is that the social scientist can gain only limited insight through the process of reflecting on their own experiences (Chamlee-Wright 2011, p. 166). Although the scientific understanding of others is fundamentally a similar process to the understanding that is exercised in the process of everyday life—in the words of Don Lavoie, “there is no difference in kind between scientists and people”—scientific interpretation is based on “extended, specialized,

and, it is hoped, critical discourse” (Lavoie 1991, p. 480).<sup>3</sup> This requires the social scientist to carefully integrate the theoretical and historical components of their task. Storr (2013, p. 93) draws on Clifford Geertz’s distinction between “experience-near concepts” and “experience-distant concepts” to describe this process. A social scientist can do a better job at trying to understand others by using their experience-distant theories to bring reason to their experience-near observations of the social behavior they are trying to understand.

The next section proceeds to discussion of a set of methods that the applied Austrian economist—and any other social scientists who deal with institutional questions—are likely to find particularly useful in their efforts to better understand.

#### **IV. The Bloomington Method of Understanding**

The Bloomington School of Institutional Analysis, founded by Vincent Ostrom and Elinor Ostrom, has been working for over fifty years with an approach explicitly designed to counter concerns about the subjective nature of knowledge and the corollary that meaningful applied research requires intersubjective understanding. Specifically, the Bloomington School emphasized field work and deep archival research as vital components of their multiple methods approach. In so doing, they acted in accord with a theoretical approach to the study of institutions that emphasized meaning and rules as understood by the actors on the ground. The remainder of this essay will explore that theoretical and practical focus through the context of the Institutional Analysis and Design Framework and its intellectual precursors, discussing throughout the

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<sup>3</sup> Lavoie even posits that the scientific use of methods, such as language, that people have created to be able to communicate ideas to each other in the process of daily life means that there is a sense in which scientific hermeneutics are modeled after agent-level hermeneutics (Lavoie 1990b, p. 361).<sup>3</sup>

relationship between this analytical approach and Austrian concerns about subjectivity and interpretation.

The great range of subjects addressed by Elinor Ostrom and Vincent Ostrom over their long careers all contributed to a single, cohesive research agenda centered around the question of self-governance; or, in other words, how people design and enforce rules to keep the behavior of themselves and others in check (Boettke, Lemke, and Palagashvili 2015). This research agenda began with an empirical puzzle that Vincent Ostrom first became interested in through casual observation of the dry Southern California landscape: with everybody drawing on a common (and not overly abundant) reservoir of water, why was there any left? (Allen 2011). Over the subsequent decades, variants of this question would be asked in the context of the ‘American experiment’ with self-government and constitutional design; the provision of local public goods, such as police services; and a variety of environmental resource issues, particularly those relating to common pool resources. The great commonality between these projects is that they are all matters of institutional analysis, where ‘institution’ is defined as a system of rules that shapes action for a particular group given a particular context.

The method the scholars in the Workshop used to study these institutional questions eventually become known as the Institutional Analysis and Design Framework, or IAD Framework (Ostrom 2010, 2011). Michael McGinnis (1999) identifies a 1965 essay as already establishing the approach that would later become more fully articulated as the IAD framework. In this early effort, the Ostroms are already chafing at the strictures of market and state. They propose thinking of governmental services as industries, where there are multiple players brought into interaction with each other by their diverse but related interests (Ostrom and Ostrom 1999 [1965]). In order to engage in analysis, then, careful understanding of the particular context

and nature of the ‘industry’ are required—simply noting that production is managed by government is not adequate. Already, the Ostroms’ work hints at the emphasis-to-come on articulating the rules of context of particular situations rather than force-fitting into a narrow set of pre-existing models and theories.

In the more developed later articulations of the IAD framework, Ostrom distinguished between three levels of analysis, the most general level of which is the framework, “...intended to contain the most general set of variables that an institutional analyst may want to use to examine a diversity of institutional settings...It provides a metatheoretical language to enable scholars to discuss any particular theory or to compare theories” (Ostrom 2010, p. 646). Specific theories and models are then developed within the context of a particular framework, making reference to components of that framework in order to explain particular relationships or outcomes or derive testable implications (Ostrom, Gardner, and Walker 1994, p. 23-27). For example, a prisoner’s dilemma is a model within non-cooperative game theory, both of which were developed within the framework of rational choice.

The IAD framework is an inherently multidisciplinary approach to the study of human institutions that begins analysis by defining the actors, rules, and context, or “action situation” (Ostrom, Gardner, and Walker 1994, p. 27-29). By beginning analysis in this way, the IAD framework denies the validity of a narrow set of organizational archetypes. In the Ostrom’s world, there is no such thing as *the market* or *the state*; rather, there are diverse institutional contexts that can only be understood by articulating the rules in effect on the ground at a particular place and time. In this way, the distinction between rules-in-form and rules-in-use is right at the heart of the IAD framework (Ostrom 2010). In specifying that it is the rules on the ground that matter, rather than the rules as recorded by a priest or a politician, we see again that

the Bloomington approach consistently distinguishes between objective and subjective conceptions of social phenomenon.

Characterized in this way, the IAD framework is an approach that is concerned with intersubjective understanding right from the beginning. Consequently, it should come as no surprise that fieldwork, archival research, and other methods designed to help the researcher develop intersubjective understanding have been critical components of the Bloomington School approach. For example, in their research on the provision of local police services, Ostrom and her colleagues took great pains to understand public safety from the perspective of the individuals living in the communities in question (see for example Boettke, Palagashvili, and Lemke 2013; Ostrom et al. 1973; Ostrom, Parks, and Whitaker 1978). They considered objective measures of public safety, such as measured crime rates, to be related but distinct from subjective measures of public safety, such as how safe citizens feel in their communities (Ostrom et al. 1978).

This distinction between subjective and objective evaluation is connected to Austrian and other hermeneutical insights about interpretation in two ways. First, if the subjective component of the phenomenon under investigation is ignored, the applied researcher may measure or evaluate the wrong thing. Measures of crime statistics and citizens' perceptions of public safety are no doubt related, but they are not equivalent, and it is the latter that will be the stronger drive to action. Regardless of what the reports say, it is an individual's subjective perceptions that will determine whether they will feel comfortable walking alone or consider moving away to a safer neighborhood. Second, the Bloomington School's recognition that purposive behavior is driven by subjective expectations directly shapes their choice of research method. The fact that subjective perception is considered important to understanding questions of public safety means

that the researcher must seek some degree of intersubjective understanding. The result is a concordance between a theoretical approach that views actors as purposive, a historical question that recognizes the subjective nature of the data of the social sciences, and a research method that enables intersubjective understanding to a degree that makes it possible to connect all three components into a cohesive body of applied research.

Elinor Ostrom's research on common pool resources is another strong example of how sensitivity to intersubjective understanding enabled her to correct the serious scientific errors made by those who approached common pool resource problems with a more specific set of theoretical preconceptions. Various models have been used to describe common-pool resources (CPRs), including the tragedy of the commons, prisoner's dilemmas, and Mancur Olson-style logic of collective action (Ostrom 1990). If a CPR situation is accurately described as a tragedy of the commons, then people on the ground should be observed to be unable to escape their predicament:

Picture a pasture open to all. It is to be expected that each herdsman will try to keep as many cattle as possible on the commons...As a rational being, each herdsman seeks to maximize his gain. Explicitly or implicitly, more or less consciously, he asks, "What is the utility *to me* of adding one more animal to my herd?" This utility has one negative and one positive component...Adding together the component partial utilities, the rational herdsman concludes that the only sensible course for him to pursue is to add another animal to his herd (Hardin 1968: 1244).

Since Hardin assumes that the only relevant decision factors are the direct benefit, which the actor enjoys fully, and the deterioration of the resource, which the actor suffers only partially, each person has an incentive to overconsume. The only solution to this problem as conceptualized by Hardin is to align the private incentives with the social incentives by designating a single responsible party. This can be done by either privatizing the resource so that the actor now bears the full cost privatization or nationalizing the resource so that the

government can charge an amount for use that will raise the private cost to the level of the social cost.

Ostrom (1990) offers a significantly different characterization of CPR situations. Through rich case study analysis, the empirical components of which are generated through a combination of field work and deep archival research, she instead finds that individuals frequently do manage to regulate their consumption without recourse to either privatization or nationalization, and have in fact devised many different, unique institutional solutions to a variety of CPR problems. Actors who find themselves in CPR situations prove to be very creative at preventing the dire consequences which these models predict. People are not 'locked into' a situation that results in ruin; instead they are successful in developing systems of rules that are appropriate for their context.

Her ability to identify and then explore this theoretical possibility is only possible because of the emphasis the IAD framework places on intersubjective understanding. Systems of rules that resolve potential CPR conflict emerge out of the interactions of various actors responding to particular problem situations.<sup>4</sup> The task is not one of deducing which rules work best in a given setting; instead the task is one of discovering which rules work well. This occurs via a process of trial and error. While researchers can describe similarities that exist across the board, it is very difficult for such a system to be created in a top-down manner.

Since the IAD framework requires the researcher to be able to identify the rules-in-use before they can identify which theories and models will be relevant for their analysis, the first step must necessarily be qualitative research. If a particular theory or model of the world is

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<sup>4</sup> See especially Demsetz (1967), who argued that, "the emergence of new property rights takes place in response to the desires of the interacting persons for adjustment to new benefit-cost possibilities" (350). We claim that systems of rules regarding the management of resources are an example of this logic in action.

decided upon before enough is known about the action situation to be sure the assumptions make sense, then whole other regions of theoretical possibilities will be cut off, and a particular set of conclusions will emerge that may or may not be consistent with reality on the ground. If the starting place of analysis is to model a CPR as a tragedy of the commons, then there is no room for the members of the community to devise their own solutions to overcome the CPR challenge. Similarly, describing a CPR as a prisoner's dilemma assumes that individuals have not succeeded in turning the game into one of coordination, and describing a CPR as following the logic of collective action assumes that societies have not developed norms that successfully align incentives. Because Ostrom instead used a framework that put intersubjective understanding first, she was able to illuminate new theoretical possibilities that had not previously been taken seriously.

The opening up of these alternative theoretical possibilities is immensely important because of the serious analytical and policy errors that can result when a problem is inappropriately defined, either out of error or out of disregard for the importance of the subjective elements of human experience. Ostrom (1990) gives the example of policy advisors armed with a model, but without the knowledge of the situation on the ground provided by qualitative methods, who recommended that developing nations nationalize the ownership of forests. The idea was that forests qualified as a CPR and that people—left to their own devices—would overuse the resource by deforesting and eroding the soil. However, in many cases nationalization of a resource actually “created *open-access resources* where previously *common-property resources* had existed” by taking away the local villagers’ sense of ownership and restraint (Ostrom 1990, p. 23; emphasis original). If policy advisers had used fieldwork as a complement to theory, they would have realized that particular models do not always apply in a

given context, and might have avoided destroying local norms that had previously governed forest management.

## V. Conclusion

As the founders of a notable school of institutional analysis, it is perhaps no surprise that Elinor Ostrom used methods that we argue can be considered as satisfying Don Lavoie's call for economists to take an interpretive turn. Institutions are systems of rules, and rules only have meaning because people believe that they matter. When considered in this way, the analysis of institutions as they actually exist—which is significantly different from analysis limited to institutional ideals—cannot be seriously undertaken by any approach *other* than the interpretive. In the words of Ludwig Lachmann, economists who do not take culture and other problems of the intersubjective seriously wind up treating institutions “like children playing with ancient coins about whose value and history they know nothing” (Lachmann 1990, p. 140).

In arguing for the role of interpretation in economic science, Lavoie created space for meaningful applied work that can be conducted in a manner consistent with awareness and care for the subjective nature of the facts of the social sciences. His approach is a corrective to the misconception that praxeological reasoning and meaningful historical interpretation are at irreconcilable odds: “There is no need for Austrians to read other people's minds or invent time machines in order to do economic history. Meaning is not inaccessibly buried in the private recesses of isolated minds; it is publicly available in all sorts of readable texts” (Lavoie 1994, p. 57). And, as evidenced by the exemplary qualitative research conducted in both the Austrian and Bloomington traditions, only a fraction of which was discussed in this essay, Lavoie was right.

So, if the interpretive turn is the proper path forward for those working in the Austrian tradition, what can we learn from the Bloomington School's decades of interpretive research? We will conclude this essay with four suggestions. First, we should engage seriously with the qualitative methods of fieldwork and deep archival research. Meaningful applied work capable of addressing institutional questions requires such. Second, as the Ostroms' lifetime of hard work and investment attest, the quest for intersubjective understanding is a difficult one. Embedding oneself in the past or in a different culture takes time and money; more time and money than many other kinds of research. However, the alternative is to severely limit the possibilities for meaningful progress in institutional analysis and other fields of questioning that require an economics of meaning. Third, and related, accomplishing the first and second objective are going to require us to master arguments in defense of these methods. Particularly in academic conversations where terms like 'intersubjective' and 'meaning' and 'qualitative' are viewed with suspicion, the ability to engage in the kind of interpretation required to do good institutional analysis is going to require a healthy dose of methodological persuasion. However, fourth, and again demonstrated by the Ostroms' oeuvre, mastery of the method and the methodological defense are mutually supporting. The IAD Framework informed their work in the field, lab, and archives, but it was also informed *by* their work in the field, lab, and archives.

In sum, the interpretive method has been offered up as a potential bridge between the theoretical abstractions of praxeology to the real world of human action. We have argued in this essay that qualitative methods, particularly field work and archival research, are the best means available to us to construct that bridge.

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