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ELEMENTARY ECONOMICS

*A Popular Introduction
of the introductory course in economic theory*

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This work briefly outlines the main principles of economic theory. It provides a framework for understanding basic terms and concepts.

The book is intended for those wishing to familiarize themselves with the terms, definitions, and fundamentals of economic theory.

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“Whether we like it or not, economic science cannot remain an esoteric branch of knowledge accessible only to a small group of scholars and specialists. Economic science deals with the fundamental problems of society; it concerns everyone and belongs to all. It is the primary and true concern of every citizen.”

L. Mises.
“Human Action .”

PREFACE

Economics — a type of human activity.

What do we mean by the term “human being,” and what is meant by “human activity”?

Without first examining these two topics, it would be premature to delve into the study of economics, which is a form *of human activity*.

At the same time, we must determine how we will verify the accuracy of various theoretical calculations regarding the topics under study. In the natural sciences, experiments are used for such verification. That is, the proposed theory is tested against the phenomena of “objective reality.” Physical laws, chemical reactions, or mathematical relationships do not depend on human opinion. Therefore, a scientist’s hypothesis can be tested in practice.

In economic theory, things are somewhat different.

Human activity gives rise to new types of relationships that did not previously exist in objective reality. Therefore, it is not possible to conduct an experiment here. After all, every experiment is, in turn, the creation of a new, unique type of relationship. Consequently, the ultimate criterion for determining the correctness or incorrectness of the propositions of economic theory is reason alone, without any recourse to experience or experimentation.

Any research conducted by a person is, first and foremost, a thought process. To describe the results of this process, each discipline uses its own language with its own vocabulary of terms and definitions.

And how is the vocabulary of terms in economic theory constructed? How is its conceptual framework formed?

And how are terms and definitions formed in general? Are there specific criteria and rules here?

The first chapter of this work is devoted to examining these questions.

CHAPTER 1. THE THEORY OF ABSTRACTION

§1. Man and Thought

Every living creature obtains food, defends itself against external threats, and ensures the continuation of its species—it acts. Actions are usually based on instincts and reflexes—both conditioned and unconditioned. This is the world and realm of the beast. A beast cannot change the goals set for it by nature, nor can it form new goals. A beast cannot act purposefully.

Man, unlike the beast, possesses a unique quality that allows him to set goals. And to achieve a newly set goal, new types of actions are needed. These are purposeful actions.

Humans acquired the ability to set new goals through their capacity *for abstraction*—to isolate and distinguish something outside themselves. This isolated element begins *to exist* for the human.

It might seem that animals can do this too. After all, a squirrel can distinguish a nut, and a fox can distinguish a hare. We know that the retinas of their eyes respond to light, and their olfactory receptors respond to scent. But we don't know whether a squirrel can imagine a nut, or a fox can imagine a hare. And we certainly don't know whether the squirrel decided on its own to crack open a nut, or whether the fox decided on its own to chase a hare? Did they have a goal, or were they merely obeying instinct and reflex?

We know only that scientists, starting with Pavlov, believe that animals are doomed to obey instincts and reflexes. Moreover, it is impossible to determine exactly where the squirrel ends and the nut begins, where the fox ends and the hare begins. It is all a single system in which signals and reactions to signals propagate. It is roughly the same as how we do not know where we end and our hand begins.

The question of whether animals distinguish themselves remains open as well. At the very least, simple observations show that in a mirror they see not themselves, but other animals. Just as a child, up to a certain age, sees not himself but another child in the mirror.

Thus, for an animal, in our understanding, nothing exists. For an animal, not even itself exists. For what exists is something distinct from itself.

In the beginning, nothing existed for humans either. There was neither the external nor the internal, nor the human itself. Everything was one, whole, eternal, and infinite. Let us call this great unity “*being*.”

Man, using his ability to abstract, has learned to isolate certain parts from this being. He can *observe* the resulting parts, that is, consider them independently of both being and himself. He distinguishes them. Moreover, to observe, in this context, does not mean to look. An animal can look, but it cannot observe.

The process of isolating and distinguishing parts of a single, eternal, and infinite existence in human consciousness is called *abstraction*.

A part of existence perceived by a human as a separate whole is *an abstraction*.

The isolated, distinguished parts begin *to exist* for the human being.

And what was the result of the first abstraction?

Through this initial act of abstraction, humanity distinguished within existence *the physical world (the observable), nothingness (the unobservable), and the self (the observer)*.

This inseparable trinity was at the beginning of everything.

The physical world — a part of existence that is discernible by human senses.

Perceptible means having boundaries. At first, the physical world was one for humans. And what lay beyond its limits, beyond its boundaries?

Beyond the boundary of the physical world was *nothingness*.

Nothingness is an important part of existence. Without this *nothingness*, we cannot imagine the boundaries of the physical world, and therefore the physical world itself. Without *nothingness*, there is nothing.

Nothingness is an indistinguishable part of existence.

Through further abstraction, humans break down the physical world into separate parts (abstractions). They perceive each of these parts as something distinct, a whole. Thus, the sun, sky, earth, water, etc., come into being for them. Each distinct (abstracted) entity begins to exist for humans.

Later, humans combine homogeneous parts (i.e., homogeneous entities) into an abstraction of a higher order—*an absolute abstraction*.

For example, at first a person distinguishes a specific apple, then distinguishes different varieties of apples, and later forms an image of the apple in general. This is how *being* emerges.

Being is a generalized image of a multitude of homogeneous existents—an absolute abstraction.

People assign *a sign* to every result of abstraction. Sounds, gestures, or written symbols can serve as signs... Abstractions and their signs form what we call *knowledge*.

Knowledge is an abstraction , translated into symbolic form.

Using knowledge, a person can construct both models of imagined events and models of their own actions. A person begins *to think*.

Thinking is operations on abstractions.

Thus, thinking consists of operations performed on entities using knowledge, i.e., using signs and images.

§2. Humans and Rules

Observing the physical world, a person continues to break it down into an ever-increasing number of existing and being entities. Accordingly, the procedure for describing the observed becomes more complex . At the same time, the shortest variants of descriptions are preserved as single word forms and are called *definitions*.

For example, if ten people try to describe the same observed object, one can obtain ten different descriptions, and all ten may turn out to be correct.

But if those same ten people are asked to construct the shortest possible description, the result will be the same for everyone. The resulting shortest version is *the definition*.

A definition is the shortest description.

A definition is always singular. There cannot be two definitions of the same observable. Otherwise, the rule of brevity would be violated.

Since the definition of each observable is unique, it can be assigned a designation, a word. *Terms* emerge.

A term is a word that denotes a definition.

Consequently, the term “*human*” must also have its own definition. Let’s try to formulate it.

A human is a being capable of abstraction.

The ability to abstract is the main difference between a human and an animal.

The constant practice of forming and applying knowledge, the practice of constructing and applying terms and definitions, develops a new quality in humans—the ability to act according to established rules. Let’s call this new ability *literacy*.

Literacy — acting in accordance with the rules.

A literate person uses terms and definitions, i.e., speaks concisely and precisely. An illiterate person, on the other hand, is forced to use rather lengthy descriptions.

Just as there are connections between phenomena, there can also be connections between objects (entities). These can also be identified and described using abstract symbols—*concepts*.

For example, there is a connection between the distance traveled and the time taken to do so. The longer you drive, the farther you go. We describe this connection with the concept of *speed*. Speed is the distance traveled per unit of time. Speed is a concept, i.e., a term denoting the relationship between the quantities of distance and time. When we hear that a car's speed was 60 *km/h*, we understand that the car traveled an average of 60 *km per hour*.

A concept is a term denoting the relationship between quantities or phenomena.

The knowledge library includes the entire set of symbols and their corresponding abstractions. These are both terms and concepts.

The ability to use knowledge allows a person to model a state that is more favorable to them than the current one. This new modeled state is called a thought. A thought becomes a *goal* when a person begins to act.

A goal is an abstract model of what is desired.

To achieve a new goal, new types of actions are needed. And these actions are no longer the result of instincts and reflexes. They are purposeful actions.

Consequently, a person is a being capable of acting purposefully. This means that there is a certain realm in which a person is free from the shackles of instincts and reflexes. Moreover, this realm is constantly expanding. Within this realm, a person gains the freedom to choose their actions.

An animal does not possess such freedom. Or, at the very least, the scope of an animal's freedom of action is infinitesimally small.

We have said that, based on the known connections between abstractions and their symbols, we can construct models of new states. The desired result we obtain becomes the goal. But how do we achieve this goal? What should we do? How should we act? After all, humans do not have pre-programmed options for action at the level of instincts and reflexes. No, because the goal has only just appeared; it did not exist before. Consequently, one must find options for new actions oneself and construct sequences of actions leading to the goal.

How do you do that?

One can use trial and error. It is a difficult and dangerous path. Or one can construct abstract models of actions and their sequences and choose the best option. That is, one can apply *analysis*.

In any case, the sequence of actions leading to the set goal that you find is saved as *a rule*.

A rule—the result of analysis—is a sequence of actions leading to the set goal.

Repeated use of the same rule leads to the formation of *a skill*. That is, a certain sequence of actions is carried out at the subconscious level, automatically. Something resembling a conditioned reflex emerges.

A skill is an action performed according to rules, brought to the point of automaticity.

Refining skills in the application of knowledge gives rise to *language*. *Speech* emerges. Speech allows a person to

communicate with another person on an entirely different level. Cooperation emerges—joint, coordinated activity aimed at achieving a common goal.

* * *

We have briefly traced the entire path of human development. A person thinks, that is, operates with knowledge. They construct abstract models of events and actions. A person sets goals that did not exist in nature before them. Humans seek ways to achieve their goals. They act. And these actions are not the result of instincts or reflexes. They are purposeful actions.

But is every human activity aimed at achieving one's goals considered *human activity*?

No, of course not.

§3. Man and the Law

The use of language to denote abstractions allows humans to interact with others on a qualitatively new level. Language allows us to share the results of our thinking and the results of our modeling of events. People gain the ability to negotiate, form groups, and act together to achieve a common goal. Thus, the ability to think abstractly became the beginning of human society. The term “*society*” has “communication” at its root.

Communication is the exchange of knowledge.

A concept is a connection between quantities and phenomena. Information is a connection between concepts.

Society is a group of people united by a common information field.

The concept “human” describes the connection of a given person with other people. As we have already said, *a concept*, unlike *a term*, describes connections between quantities and phenomena. It is dynamic. This means that the concept of “human” is also dynamic; it changes.

Once upon a time, it was enough for the first human to simply have the ability to abstract in order to be called a human. A “term” was sufficient. There was no need to distinguish a “concept.” One could say that at first, there was only one human. That is, he was able to distinguish himself, to set himself apart from existence. And now, in the reflection in the water, he sees himself. And he alone is human. There are no others yet. Since he does not yet distinguish them.

But over time, the ability to abstract and the constant practice of interacting with others like himself allowed a person to distinguish another person.

This was a very significant transition. The individual himself, of course, was not aware of it. It was simply a process of natural selection that had been set in motion. After all, if one can communicate with another person—that is, exchange knowledge—then it becomes possible to reach agreements and act in concert. And this greatly increases the likelihood of survival. Consequently, certain rules of communication and interaction between people began to emerge, which more successfully led to the achievement of goals. As these rules developed, so did the very concept of “human.” The criteria distinguishing “human” from “non-human” began to change. These changes occurred in leaps and bounds, from one level to the next.

Quantum philosophy is taking shape.

§4. Quantum Philosophy

There is no continuity in the development of the human being and human society. It occurs in leaps. Leaps from one level of abstraction to another. Each new human level is formed by a new way of distinguishing: who exactly is to be considered a human being.

At first, “people” are only members of one’s own family. Later, they are members of one’s own clan or tribe. Still later, they are members of one’s own nation. Next, they are all fellow believers. And finally, all those who have renounced violence against any other person are members of what is called *civil* society.

Every significant change in the requirements for human qualities can be identified as a transition to *a* new human *level*.

People at different human levels can coexist in the same territory at the same time. Every person also passes through the corresponding human levels from the day of their birth.

The transition from one level to another occurs in leaps. The history of the individual and of humanity is discrete.

Thus, the ability to think abstractly has allowed humans to create their own human *world*.

In this human world, as a result of thousands of years of activity by countless generations of people, a fundamental rule and a fundamental prohibition have taken shape—the

prohibition against the use of *violence* against another human being.

For it is precisely the rejection of violence against human beings that created this human world.

§5. Politics and Law

What is violence, and how can one distinguish whether violence occurred or not?

Violence is force applied against a person. Force is, first and foremost, a physical action exerted on a physical object.

The physical aspect of a human being is their body. Therefore, violence is primarily defined as a physical impact on the human body. Consequently, the use of force to restrict a person's ability to use their body is also violence. Thus, restricting a person's ability to act—including to act purposefully—is also violence.

The ability to act purposefully is called *freedom*. This means that forcibly restricting freedom is always violence.

Purposeful action is action according to rules. Rules are formed by humans. The ability to act according to one's own rules is called *a right*.

Consequently, the coercive restriction of *rights* is also violence.

To achieve a goal while acting according to rules, a person uses resources. This includes resources obtained through human activity. This is *property*. The forcible seizure of property or the forcible deprivation of the ability to use property is also violence.

In general terms, we can state:

Violence — the use of force against a person, i.e., against their freedom, rights, and property.

Violation of this rule is today regarded as a rejection of humanity (in the sense of its highest level).

How did this rule come about? How did this prohibition arise? And who imposed this prohibition?

Of course, the prohibition on violence was not imposed by a chieftain or a king, nor by a popular assembly. This prohibition arose as an unintended result of the activities of many generations of people.

In many isolated communities, their own rules of communication and interaction form spontaneously (unintentionally). Which of them will prove to be the most successful, in terms of preserving and growing the community, no one knows in advance. It is impossible to know this in advance.

The most successful rules are preserved, just as the communities in which they arose are preserved and thrive. One could say that the rules chose the community, rather than the community choosing the rules.

Over the millennia, one fundamental rule has emerged: the prohibition against the use of violence. It is precisely this prohibition that has enabled human society to survive and thrive. And this prohibition is universal in nature. It makes no distinction based on skin color, social status, gender, or age. This is *the law*.

The law is a formal prohibition against the use of violence against a person.

As we have already said, human laws cannot be adopted by a vote or established by force. They can only be

discovered, revealed. Much like the laws of physics are discovered. After all, the laws of physics are not adopted by a vote of scientists. Scientists merely discover them. Nature will not submit to arbitrarily established laws. And coercing people to submit to these laws by force leads to nothing good.

Thus, the law is a formal prohibition on the use of violence. Moreover, the law clearly distinguishes between *force* and *violence*. The law establishes limits on the use of force against a person.

Thus, the law protects people from violence. To defend oneself, one may use force. And in this case, it will not constitute violence.

Defense is the use of force against violence.

Politics is the organized use of force to protect people.

In most cases, force is used to protect a person at a higher human level from violence by a person at a lower level.

For example, for a person at the “tribe” level, a member of another tribe is not “one of their own” and is not considered human. Consequently, the use of violence against them is permitted. But for a person at a higher level—for example, at the “nation” level—all tribes that are part of their nation are “one of their own.” That is, members of other tribes are also “one of their own” and are considered human. Violence cannot be used against them.

It is clear that a so-called civilizational conflict arises between people who remain at the “tribe” level and those who have risen to the “nation” level.

Civilization — a society protected by politics, i.e., a society in which an organized system of human protection against violence has been established (from the Latin civilis — fenced in, protected).

A *civilizational conflict* is a conflict between representatives of different human levels, a conflict between the rules of distinction between “human and non-human.”

Every person sequentially passes through these same levels of civilization from the day of their birth until they reach adulthood.

At first, a child distinguishes only members of their family. A little later, they become acquainted with other relatives. Then—with neighbors. Then—they distinguish nationalities and languages, distinguish affiliation with various beliefs... and so on.

The purposeful influence on a person to raise them to a higher human (civilizational) level is called *upbringing*.

At the modern level, at the level of “civil society,” the concept of a human being can be formulated as follows:

A human being — a being who recognizes another human being and acknowledges their rights, freedoms, and property.

CHAPTER 2. HUMAN ACTIVITY

§1. Goals and Benefits

The ability to think abstractly has enabled humans to analyze the present and model the future. The primary motivation for this kind of modeling is a sense of unease regarding the current or future state of affairs. Such unease is triggered, for example, by any threat to life.

Anxiety and fears also arise when it is impossible to understand the connections between phenomena, and thus impossible to analyze the current or future state of affairs. Uncertainty is one of the factors causing intense anxiety.

In an attempt to alleviate anxiety, a person models new situations. A model of a new situation (a thought) that is successful from the person's perspective, constructed as a result of thinking, becomes *a goal*.

If a state (goal) is found in which there is less anxiety, a person, again using models, assesses the risks of transitioning from the current state to the preferred state. In most cases, a person begins to act when satisfactory models of the proposed actions leading to the desired result are obtained.

The ability to set goals has given rise to a completely new type of activity—purposeful activity.

To achieve a newly formed goal, it is necessary to develop new types of actions that did not previously exist in nature. These actions include interaction with other people.

But for a person, as we have already said, the use of violence against another person is out of the question. Consequently:

Human activity is activity aimed at achieving set goals without the use of violence.

Most new types of actions require additional energy expenditure. Moreover, mental activity itself also requires additional energy expenditure. And the search for or acquisition of such energy is not provided for in the old instincts and reflexes of the animal world. Humans are forced to acquire it themselves.

The sources of energy used by humans in their activities are called *resources*. New types of actions require new resources.

The resources used by humans to achieve a goal are called goods.

The resources available to humans are limited. Consequently, new challenges arise: how to obtain the necessary resources, and toward which specific goals should they be directed first and foremost? The ability to think abstractly allows humans to solve these challenges as well.

First, the simplest and quickest method of achieving the goal—at least at first glance—is modeled and evaluated in terms of available opportunities and resources. If the result is unsatisfactory, the next model is constructed. In each new case, both ways to use existing resources more effectively and opportunities to acquire new ones are explored.

§2. Ethics

Suppose a person has decided that the course of action they have found can lead to the desired goal and that the necessary opportunities and resources are available. Nevertheless, they do not act automatically.

Before acting, a person also assesses the risks associated with their reputation. That is, a person evaluates their actions and their results from the perspective of other people as well. After all, connections with others, as well as interaction and cooperation with them, provide immeasurably more opportunities. It is undesirable to risk these connections for the sake of a private, temporary benefit. New rules are being developed to regulate human activity. They have nothing to do with force, that is, they have nothing to do with either violence or defense. These rules have been called *ethics*.

Ethics are the rules governing non-violent human interaction.

At the same time, ethical rules (or norms) constitute a spontaneously emerging, rather conservative, and inert system for regulating relationships between people. They develop over a long period of time.

The internalization of ethical norms occurs at an early age and, for the most part, unconsciously. Thus, human behavior is determined to a significant extent not only by the individual themselves, but also by the norms, rules, and laws embedded in their consciousness.

Nevertheless, there is always a certain area in which each person makes their own conscious choice.

§3. Experience

And what happens if the anxiety is strong enough, yet one cannot construct a model to alleviate it? What should one do if there is no initial data or the necessary abilities for such an analysis?

In this case, some people resign themselves to the anxiety, while others begin to act. To act without rules, that is, spontaneously. Such unmodeled actions are called unintentional. They, too, yield some result.

If the result is positive, data necessary for modeling further actions is accumulated. If the result is negative, this is also a result that is taken into account when constructing future possible courses of action. *Experience* is accumulated.

Experience is the connection between objects or phenomena obtained as a result of unintentional actions;

A.S. Pushkin called experience “the son of difficult mistakes.”

To gain experience through spontaneous actions that cannot be calculated in advance or simulated, special qualities were required. After all, negative experience, no matter how valuable it may prove to be for others, could prove fatal to the person who experienced it.

An unintentional action leading to the acquisition of experience is a kind of *sacrifice*.

§4. Praxiology and Economics

The goods available to a person are limited, while goals are numerous. Consequently, a person must, first, decide how to obtain the missing goods, and second, choose how to allocate them among competing goals. After making a decision, a person must act. Otherwise, the goals will not be achieved. But action must remain within the bounds of rules prohibiting violence. Otherwise, a person ceases to be human. Violence must be excluded from the possible courses of action.

Human activity is, by definition, nonviolent.

The theory describing the optimal ways to achieve established goals is called *praxeology*.

Praxiology is a theory describing the optimal ways to achieve established goals, or the science of human activity.

Praxiological analysis is the search for ways to achieve a set goal.

Since a set goal is the result of mental activity, praxeological analysis is also the result of human mental activity and mental activity alone. And this analysis is based not only on one's own evaluative judgments but also on the evaluative judgments of others. Therefore, certain rules and limitations may apply here.

Goal-setting is also a cognitive process. But there can be no rules or restrictions here. After all, no one knows in advance what the meaning of life is, or what its ultimate true goal is. Therefore, everyone has the right to set and pursue the goals they deem necessary, in the way they deem necessary.

An integral part of praxeology is the study of methods for acquiring and distributing goods to achieve a set goal. This part of praxeology is called *economics*.

Human activity aimed at obtaining goods and distributing them among the established goals according to their rank of importance is called economic activity or simply economics.

The process of setting the goals themselves is not the subject of praxiology or economics. That is the domain of *psychology*.

§5. Economics and Ethics

Variants of successful methods for solving economic problems are preserved and accumulated in the form of rules. Following these rules makes the achievement of the goal more likely.

For quite a long time, physical survival was the primary factor for humans. Increasing the resources available to sustain and prolong life was the most important activity. Anyone who found a way to increase the available resources attained a higher social status.

Cooperation and joint activities yielded greater benefits, provided greater security, and ensured a longer lifespan. Consequently, the most successful variants of cooperative rules began to be preserved and accumulated. Moreover, their selection and preservation were not conscious processes. No one could know or calculate in advance which specific rule would prove useful.

Due to differences between social groups inhabiting various territories, the rules of cooperation that spontaneously emerged within them varied greatly.

The best rules, discovered by chance, enabled the groups that discovered them to survive and thrive. Over time, as they grew in number and power, they displaced other groups. In this way, the most successful rules of cooperation among people spread unintentionally.

These rules began to take shape not only as laws but also as norms of ethics, morality, and virtue. Moreover, the fully understandable and distinguishable signs of a discovered rule's usefulness were not the opinions of authorities or the arguments of moralists, but rather the increase and preservation of a fully tangible benefit. The benefits obtained as a result of following established rules came to be called *wealth*. By "rules," we mean, first and foremost, commandments. Commandments are given by God. Hence, wealth is a benefit given by God. Benefits obtained through violence are not considered wealth.

Human activity aimed at setting new goals and developing new ways to acquire the goods necessary to achieve them is called *entrepreneurial* activity or *labor*.

It is precisely this human activity—entrepreneurial activity, and no other—that has made the survival of a colossal number of people possible, lifting them out of poverty and hunger. And it is precisely this that is the main factor *in philanthropy*.

Consequently, every active person, while pursuing their personal goals within the framework of human activity, unwittingly contributes to the strengthening of morality and the expansion of the body of social norms, which form the basis of ethics.

Advocates of the “reasonable and fair redistribution of wealth in favor of the needy” only destroy these rules, which have developed over millennia, and increase the number of people in need.

§6. Economics and the Natural Sciences

A person engaged in economic science constructs a theory that describes activities aimed at acquiring goods and activities aimed at distributing goods among established goals. Moreover, these are activities that exclude violence.

Economic theory is built on the identification (discovery) of general patterns in how people form evaluative judgments regarding possible ways of acquiring and distributing resources.

The study of the patterns governing the formation of the goals themselves is not part of economic theory.

How does economic science differ from the natural sciences, such as physics? How do the regularities discovered in economics differ from the laws discovered in physics?

A physicist proposing a description of the relationships between phenomena cannot influence the phenomena themselves in any way. Newton cannot influence gravity, nor can Ohm influence the dependence of current in a conductor on voltage. Here, the observed phenomena themselves become facts that must be taken into account. Correspondence with the facts serves as the test of the validity of the proposed calculations. A physicist cannot exert force against the observed and studied phenomena. And the relationships between phenomena do not depend on the evaluative judgments of the physicist-researcher.

In economics, things are somewhat different. Here, everything depends on individual evaluative judgments. And here, in human relationships, violence occurs, which can force a change in evaluative judgments or even force one to act contrary to evaluative judgments.

If we conditionally isolate violence—that is, if we consider human activity in its pure form—individual evaluative judgments still remain, and these are subject to change.

But there are as many individual judgments as there are people, and they are constantly changing. It may seem that in reality it is impossible to construct an adequate general economic theory.

Physicists studying the state of gases once faced a similar problem. There are many gases; they are different, and it seemed that a theory had to be constructed for each gas separately. Each gas consists of individual molecules; they interact, and the result of this interaction depends on their relative speeds. And the speeds of the molecules are different and constantly changing. Therefore, a theory describing the state of even a single gas turned out to be incredibly complex.

A solution was found in the development of an *ideal* gas model and the application of methods from mathematical statistics. A theory for the ideal gas was quickly formulated. It allowed for a reasonably accurate description of the state of a real gas by incorporating corrections for the real gas into the laws governing the ideal gas.

In the same way, economic theory sets aside not only violence but also an infinite number of individual evaluative judgments, replacing them with an average value derived from the discovery of certain regularities.

What are these regularities, and where were they discovered?

Generally, people prefer to be healthy and wealthy rather than poor and sick. And people generally prefer to use a certain resource today rather than have the opportunity to use it in an uncertain future. People also generally wish to obtain what they desire at the lowest cost of their resources and, if possible, in the shortest time. These are all regularities common to the majority. Economic theory relies on them, just as mathematical theory relies on postulates.

But while a mathematical postulate is considered unshakable and always holds true, an economic postulate is always relative. There will always be an exception to the rule where a given economic postulate may not hold. That is, economic theory deals with uncertainty.

Economic theory strives to reduce this uncertainty, but it cannot completely eliminate it. Clearly, it is not the theory that strives, but the person constructing the theory; however, for brevity's sake, let us say that the theory strives.

People usually fear uncertainty. They desire certainty. That is why theories often emerge that purport to establish such certainty. But one must understand that constructing such a theory is impossible, just as it is impossible to build, for example, a perpetual motion machine.

§7. Calculations and Measurements in economics and mathematics

A measurement is a comparison with a standard. A *standard* is a homogeneous quantity taken as a unit of comparison.

A quantity is the result of a calculation or measurement. In the natural sciences, quantities are often

denoted by letters (parameters). The relationship between quantities, expressed in terms of parameters, is called a *formula*.

The formula allows us to calculate what is difficult to measure using what is easy to measure... For example, by measuring the diameter of a circle, we can calculate the circumference using the formula $c = \pi d$. This formula holds true for any circle. It is impossible not to agree with the result of this calculation.

In the natural sciences, standards are universal, and relationships (formulas) are objective. The formulas for the circumference of a circle or the law of universal gravitation do not depend on a person's subjective judgment.

Economic quantities differ from mathematical or physical quantities. Economic quantities are the result of subjective judgment. Therefore, the results of calculating economic quantities using the proposed formula may differ among different people.

To resolve conflicts regarding the results of such "calculations," the parties agree each time on what exactly to consider the standard within the framework of the current transaction and which relationships (formulas) to consider valid. There are no universal (objective) standards or formulas in economics. Mathematical calculation is impossible here. Nevertheless, economic calculation does take place. It will be discussed in more detail in the chapter "Market."

§8. Simulation of Human Activity

Human activity is, by definition, nonviolent. Cooperation among people based on nonviolence, on a contract voluntarily accepted by both parties, yields phenomenal results.

The quantity and quality of available goods grow immeasurably.

At the same time, when cooperation breaks down and violence is used, universal decline sets in.

People who use violence—bandits, thieves, swindlers, etc.—may, as a result of their actions, gain temporary, private material benefits. But this benefit becomes negligible if those around them can recognize the true nature of their actions. Therefore, a kind of mimicry develops among violent people—***the imitation of human activity***. Bandits use the same terms as honest people to describe their “activities.” They, too, seem to have jobs, businesses, profits, losses, salaries, professions, companies, services, charity, the economy, and so on. For the average person, in this case, it is difficult to figure out exactly what they are dealing with. After all, in reality, robbers have no profit—they have loot. And robbers have no work—they have robbery.

It is very difficult for an untrained person to recognize the imitation of human activity. After all, on the surface, everything seems respectable: smiles, politeness, a company, paperwork, concern for the environment, and the fight against climate change... Nevertheless, it may all turn out to be nothing more than an imitation. Its metastases imperceptibly devour the healthy fabric of society, and at some point, crisis, famine, and wars ensue.

Early detection of imitations of human activity is becoming quite important for every honest person. Can this be learned? Of course it can. One simply needs to understand economics and the theory of abstraction. To do this, it is enough to be honest with oneself, accept the conclusions of formal logic, and rely solely on one’s own mind to analyze

events. To begin with, it is advisable to learn quantitative analysis of the relationships between measurable quantities and events within the framework of 7th-grade high school mathematics. After that, one can truly begin to follow the words of L. Mises:

“Whether we like it or not, economic science cannot remain an esoteric branch of knowledge accessible only to a small group of scholars and specialists. Economic science deals with the fundamental problems of society; it concerns everyone and belongs to all. It is the primary and true duty of every citizen.”

We must find the time, energy, and resources for the primary and true duty of every citizen, just as we find the time, energy, and resources for daily hygiene.

CHAPTER 3. PROPERTY

§1. The Entrepreneur and the Common Good

An individual typically prefers to expend as little effort, time, and resources as possible to achieve a goal. At the same time, no one knows in advance the method that is guaranteed to ensure success in achieving the goal.

External, physical resources are inexhaustible. The material world is infinite. But the resources that can be converted into goods—that is, those available to a person—are limited. Goods must be acquired. And a person usually wishes to spend as few of their available goods, efforts, and time as possible on acquiring new goods.

A person who is engaged in seeking the resources necessary to achieve a goal they have set for themselves is called *an entrepreneur*.

An entrepreneur is a person engaged in economic activity. That is, a person who wishes to alleviate some anxiety through purposeful activity that changes the existing state of affairs.

Resources are needed to conduct economic activity. Recall that the resources used to achieve a goal are called *goods*. The property of a good used by a person to alleviate anxiety is *the utility* of that good.

A person's evaluative judgment regarding the utility of a good is called *the value of* that good.

If a person is deprived of a good that is valuable to them, their anxiety increases. Acquiring a valuable good reduces their anxiety.

Goods available to a person are divided into limited and unlimited.

A good is called *unlimited* if the consumption of any part of it does not cause it to diminish.

A good is called *limited* if the consumption of any part of it causes a significant decrease in the good as a whole.

Different goods possess different levels of utility. By evaluating the utility of a good, a rational person determines its *rank*, i.e., its value relative to the value of other goods.

If food and water are abundant, their value to a person decreases. It decreases because their quantity does not cause concern.

If supplies run low, the person, anticipating the future, realizes that tomorrow there may be a famine. This prompts him to act—to build up food reserves. But any activity requires the expenditure of goods, both internal and external. In this case, for an additional amount of food, they will be willing to sacrifice a greater amount of other goods; that is, the value of food to them increases.

A person doesn't worry that they might run out of air tomorrow, even though they couldn't survive for even five minutes without it. Here, using any amount of air does not lead to its depletion. In this case, air is an unlimited resource. Its scarcity is very high, but its value is practically zero. There is no need to expend other resources to extract it or deliver it to the point of consumption.

A person living on a large lake does not worry that he might run out of water tomorrow. His consumption of any amount of water does not reduce the total amount of water. The utility of water is high, but its value is low. However, unlike air, water does have some value here. After all, water must be transported to the point of consumption. This requires the expenditure of other resources.

A person living in the desert is constantly worried about the availability of water supplies. Here, water is a rather scarce resource. To extract it or deliver it to the point of consumption, one must expend many other goods. The value of water for a person in the desert is very high.

In every case, the value of a given good can be measured as the smallest amount of another good required for its extraction and delivery.

The utility of gold compared to water or bread is quite low. But its value can turn out to be very high.

Gold alleviates anxiety about the availability of goods in a system with developed trade. With a small supply of gold, one need not worry about bread and water.

In a system where trade is underdeveloped, however, gold items serve as markers of social status. These markers alleviate anxiety about personal security.

Gold is a scarce resource. Its extraction and transportation—converting it into a benefit—require the expenditure of a large quantity of other goods. Hence its high value. Much higher than the value of bread.

But life is dynamic. And when the situation changes, when the quantity of available goods changes, people reassess their value. If food supplies have dwindled significantly, they are ready to trade gold for bread.

Thus, for a rational individual, there is a constant process of reordering the value of goods according to their importance. This is done to make the most efficient use of scarce resources.

Maximum efficiency in the use of scarce goods is achieved by converting them into property.

§2. Property

The general term for external and internal scarce goods used by people in economic activity is called *property*.

Property is a good acquired as a result of human activity.

How does a person acquire resources to achieve their goals? Where do they obtain goods? How is property acquired?

Let's consider a model describing the ways in which a person acquires goods, i.e., property. There are five such ways.

1. Initial discovery and introduction into economic circulation.

The oldest way of acquiring property is *gathering* and *hunting*. In the early stages of human development, gathering was most likely the primary means of acquiring the resources necessary to achieve one's goals. Consequently, the number of goals was also very limited. Primarily, the goals were finding food and organizing self-

defense—that is, the same as for any animal. Here, the head of the family single-handedly sets new goals and manages resources. He also uses family members as his own resources.

Over time, the more determined and enterprising individuals manage to accumulate sufficient resources and experience. This, in turn, increases their lifespan and allows them to pass on their experience to the next generation. Experience is preserved in the form of traditions. The family grows.

2. Inheritance.

Large families have the opportunity to accumulate and pass on more resources and more experience to their heirs. Consequently, both the resources accumulated by previous generations and their experience are passed on to the new generation. This is *inheritance*.

Thus, both physical and intellectual resources accumulate within the family. Over time, the amount of resources available to a person increases. This allows for more successful achievement of old goals and the formation of new ones.

Since different families in different regions use different methods of acquiring, distributing, and conserving resources, over time, some families that have accidentally discovered more successful methods end up with more resources. These families grow in number, as they are able to feed a larger number of their members. They preserve and pass on to future generations the most successful rules of

resource management. The family expands and becomes a clan.

The head of the clan is responsible for setting new goals and allocating key resources. He treats the heads of households as a type of resource.

3. Production.

Individual families may specialize in a single type of activity and develop more skills. Specialization also involves the manufacture of tools that make the work easier. Tools make it possible to produce the necessary resources in larger quantities. Families engaged in specific types of production stand out.

Resource production, unlike gathering, is less susceptible to external conditions. Therefore, a clan can accumulate and utilize far more resources than scattered groups of families. The clan begins to grow in numbers and split into a group of clans. A group of clans forms a tribe. In the tribe, the tribal chief and the clan elders participate in setting goals and distributing resources (). Their activities are strictly bound by traditions and customs—spontaneously emerging rules for the use and inheritance of scarce resources.

4. Exchange.

In various territories, different tribes gradually form, each possessing significant resources. However, the quantity and type of these resources still depend on the geographical and natural conditions of their habitats. In some places, there

is an abundance of timber and furs; in others, water and fish; and in still others, stone and ore. A resource that is scarce in one area may be readily available in another. However, due to great distances, information about this remains inaccessible. This is the case until interaction is established between neighboring tribes. Scarce resources begin to flow along a chain from tribe to tribe over fairly long distances. This becomes possible as a result of the emergence of a new way of acquiring resources—*exchange*. Property set aside for acquiring new resources through exchange becomes a commodity.

A commodity is a portion of property set aside for exchange.

Exchange between different tribes that are not related by blood gradually blurs the boundaries between them and unites them into a new social group—a nation. Here, the centralized setting of goals and allocation of resources becomes quite difficult due to the large population and vast distances.

A new means of acquiring resources—trade—intensifies the division and distribution of labor. Trade is an indirect exchange.

Local centers of craft production and trade emerge, free from patriarchal clan relations. These are cities. In the city, private property emerges for the first time, something that was unthinkable in the earlier patriarchal era.

5. Gift.

The city allows significant resources (property) to accumulate in the hands of individual people. They may transfer part of their property to another person without exchanging it for another good, as a sign of special regard for that person. This is *a gift*.

In each of the five cases discussed above, a person acquires a benefit without the use of violence, i.e., within the framework of human activity. A person may dispose of the benefit obtained in this way at their own discretion, including for economic activity.

The emergence of property is an unintended result of human activity. Property did not arise at anyone's behest or by contract. There were no decrees or edicts that introduced the concept of property. How, then, did it come into being?

The conversion of scarce resources into private property, as already mentioned, allows them to be used with maximum efficiency. Consequently, those communities where rules establishing and protecting private property arose spontaneously came to possess greater economic and military power. They began to multiply in number and expand geographically. This, in turn, led to the preservation and spread of these rules.

CHAPTER 4. CAPITAL

A person can and does set aside a portion of their resources for later consumption. This is *simple saving*.

The future is uncertain. This uncertainty about the future drives people to make simple savings. If people knew that the situation in the future would be exactly the same as it is today, there would be no need for simple savings.

A person may set aside a portion of resources for production or exchange. In this case, the resources set aside are referred to as *capital* (Latin: **capital**—head)¹.

Since production and exchange can be used for the direct consumption of their results, a more precise definition of *the term "capital"* would be:

Capital (term) — a portion of property used to generate profit.

On the other hand, *the concept* of capital represents a connection between the problems of current activity and possible methods for solving them in the future. This connection is identified by assessing possible consequences from the perspective of a specific plan and within the

¹ Most likely, the word "capital" derives from the word "kopa." A kopa is five dozen (60) and is used when counting on one's fingers. Before the decimal system, the sexagesimal system was widely used. A kopeck is one-sixtieth of a unit, specifically one-sixtieth of a hryvnia. From this comes the verb "to accumulate." The result is "capital."

framework of a specific model. The concept of capital is a praxeological concept. It is a product of thought.

Consequently, one must distinguish between the concept of capital and the term capital.

Capital (concept) is the result of a comparative analysis of the current and possible state of affairs.

In fact, an entrepreneur models the future. He thinks, that is, he operates with abstractions. He has information about the current state of affairs. If it causes concern, the entrepreneur begins to construct models of a possible state, one that is more preferable than the present. Knowledge of current resource prices and an understanding of possible future resource prices help him build such models. But he relies on more than just prices. The entrepreneur also builds models of ways to use resources to improve the situation—that is, he develops new technologies. This is his intellectual resource—capital.

While information about market prices is the same for everyone and accessible to all, the best ways to extract resources and the best ways to use them are always the result of individual decisions. This ability is also a form of capital. It varies among different entrepreneurs. This capital may be in demand in the market, which means it has value.

Consequently, to change an existing business, expand it, or start a new one, it is not enough simply to have additional resources. One must be able to envision exactly how to expand the business, and one must figure out exactly what new business to start and how to properly allocate available resources for that purpose.

Thus, capital is a complex phenomenon that encompasses both a person's resources and their ability to construct and analyze models of the future.

A person who lacks sufficient capital—both in terms of resources and abilities—can acquire it on the market.

CHAPTER 5. PROFIT

A person uses part of their available resources to obtain other resources. We can observe the earliest examples of this among herders and farmers.

A herder uses part of his livestock to increase the herd. The difference between the number of animals received and the number originally owned is called the increase.

A farmer uses part of his grain to sow and obtain a greater quantity of grain. The difference between the amount of grain received and the amount sown is called the harvest.

The difference between the amount of goods used and the amount of goods received is usually called profit. But profit, as an economic term, is a bit more complex.

Let's take a closer look at exactly what goods a person uses to produce new goods.

First and foremost, of course, these are the natural resources obtained through the five methods described above, and these are *external resources*.

A person uses another type of resource in their activities, consisting of their own time, their own physical energy, and their own intellectual abilities. These are also resources. We have called them *internal resources*.

§1. Initial Percentage

Human activity unfolds over time. It is dynamic. Therefore, each of the available resources can be used either

immediately or in the future. And every person usually prefers to get a result today rather than in an uncertain future.

Consequently, a person values the opportunity to use a resource to satisfy their needs in the near future more highly than the opportunity to use the resource in the more distant future. Their ratio, expressed as a percentage, is described by the initial percentage.

This can be illustrated with an example.

A person with the necessary funds prefers to buy a car today rather than postpone the purchase for a year. Consequently, the value of the car today, all else being equal, is higher to them than the value of the same car a year from now. But this does not mean at all that the car will cost less a year from now than it does today. As we noted—all other things being equal. In a year, the car will cost the same as it does today—this is the condition of the problem.

If the car costs, say, \$25,000 today, then we'll assume it will cost the same amount a year from now.

So what changes for our buyer? Today, he is willing to pay \$25,000 on the condition that he receives the car today as well. But he is not willing to pay that amount today if he will only receive the car a year from now. It turns out that, for him, the car he will only be able to use a year from now is worth less. By how much?

Let's say he values the car he can use in a year at \$20,000. But this is compared to the option of getting the car today—and only for him. If he goes to the dealership exactly one year from now, he'll have to pay the full \$25,000.

If we divide 20,000 by 25,000, we get $\frac{4}{5}$ or 0.80.

That's the same 80%. Is that the initial percentage? But is that really how it's calculated?

Of course not. In reality, the buyer isn't assessing what the car's value will be a year from now. He's assessing something else. If someone asks to borrow that \$25,000 for a year, it means the owner of that money would have to postpone buying the car for a year as well. Under what conditions would he agree to that?

Let's say they agree to lend the money on the condition that, in a year, they'll be repaid, say, \$30,000. The \$5,000 difference is the cost of forgoing the satisfaction of their need for a new car today.

Consequently, he is willing to save (not spend on a car today) \$25,000 if he expects to receive an additional \$5,000 in a year. And this \$5,000, in his view, is enough to outweigh the benefits expected from spending the entire \$25,000 to satisfy his need for a car literally today.

If this situation repeats itself every year, then the \$25,000 becomes permanent capital for its owner.

So, the owner of \$25,000 has decided that the value of satisfying his need for a car today is \$5,000 higher than the value of satisfying it a year from now.

How did he calculate this difference?

He didn't calculate it. It's impossible to calculate. He simply assessed it that way. And the initial interest rate is derived from this assessment. It expresses the value of deferred consumption relative to the value of immediate consumption.

In our case, the value of immediate satisfaction of the need (not the cost of the car) is \$5,000. And the value of deferred consumption (the cost of the car) is \$25,000. What percentage of the value of future consumption does the value of immediate consumption represent?

$$5,000 : 25,000 = 0.20.$$

Therefore, the initial percentage is 20%.

The initial rate is the value of immediate consumption per unit of deferred consumption.

The initial rate is not the price of capital or capital goods. Its value does not depend on the volume of their supply and demand. It is a human judgment. Rather, the initial interest rate itself determines both the demand for and the supply of capital and capital goods. It determines what portion of the available stock of goods should be directed toward consumption today, and what portion should be set aside to provide for more distant periods in the future.

But people save and accumulate capital not because interest exists. The initial rate of interest is neither the driving force behind saving nor a reward or compensation granted for refraining from immediate consumption. It is merely a description of the fact that a person prefers to satisfy needs in the near future rather than in the distant future. The initial interest rate is simply the ratio of the relative valuation of present goods to future goods.

§2. Wages

Every person possesses a set of internal and external resources that they can use to achieve their goals. A person acquires internal resources in exactly the same way as external ones. That is, they are also acquired through the five well-known methods: discovery, production, exchange, inheritance, and gift.

In fact, the physical qualities of the human body are largely inherited or developed through years of training.

Moreover, the services of a master trainer can be paid for, meaning that physical qualities can be obtained in exchange for an external resource. Similarly, intellectual resources can be discovered independently, developed with the help of a teacher through study, or inherited from parents.

Consequently, we can identify cases where a person exchanges their internal assets for external resources. In this case, we say that a person is hired for a job and receives a salary. That is, as payment for their used internal resource, they receive an external resource. This will be their salary.

Simple profit is the difference between wages and the internal resources expended

§3. Entrepreneurial profit

, by modeling situations using abstractions, can identify a state more desirable than the one in which he currently finds himself. This new state becomes his goal.

The transition to the new state requires the expenditure of resources. These are limited. The entrepreneur models possible ways of acquiring the necessary resources.

To build these models, he uses known value ratios established in the market and the anticipated ratios between them that may arise in the future. This includes those resulting from his own, the entrepreneur's, activities. This modeling of the future is called *speculation*.

Speculation is the modeling of future supply-and-demand relationships in the market.

Based on the results of this modeling, the entrepreneur begins to act.

If the speculation proves successful and the value received exceeds the cost incurred, the resulting positive difference is called *entrepreneurial profit*. If, however, the difference turns out to be negative, it is called *a loss*.

The sole source of entrepreneurial profit is the entrepreneur's ability to model and forecast future consumer demand better than others.

The source of entrepreneurial profit and loss is the uncertainty of the future balance between supply and demand. A well-constructed model allows the entrepreneur to reduce this uncertainty for themselves.

§4. Gross Profit

To achieve their goals, people use available internal and external resources. If available resources are insufficient, they attempt to acquire them. To do this, they use, among other things, trade. That is, they allocate a portion of their resources to obtain new resources. The difference between all resources received and resources expended constitutes their *gross profit*.

Gross profit is the difference between the benefits received and the benefits expended to obtain them.

Thus, gross profit consists of simple profit, initial interest, and entrepreneurial profit.

CHAPTER 6. THE MARKET

§1. The Fair and Formal Rules

In closed patriarchal-communal societies, trade does not arise. In prehistoric times, the bulk of resources is at the disposal only of heads of families, clans, or tribal chiefs. They alone are also responsible for setting new goals. They worked together and ate together from a common pot. There is no private property yet.

Each community has its own relatively stable boundary, which is defended against encroachments by outsiders. Nevertheless, there is interaction between the leaders of neighboring communities, accompanied by the exchange of gifts. These gifts may include rare items that have traveled a long way. That is, in the first stage, “goods” move, while the owners of the “goods” do not. And exchange occurs only between groups that are strangers to one another. The exchange of resources developing between neighboring communities gradually strengthens the ties between them and gives rise to a new common language of exchange.

Different exchange rules develop among different communities. The most successful rules are preserved, as the communities that discovered and adopted them are preserved and develop.

The uniqueness and high utility of certain “goods” received as gifts from a neighboring tribe prompt the dispatch of a special group of people to seek them out. To travel through

the territory of neighboring communities, appropriate gifts and guides are needed. A portion of the total produce is allocated for this purpose. The specific route and destination of such an expedition may not be fully known or understood at the initial stage.

Nevertheless, a successful expedition can bring the community many valuable resources that cannot be obtained any other way.

Expeditions become regular. Expedition routes become increasingly diverse and distant. Now it is not the “goods” themselves that move between communities, but rather they are transported by special groups of people. This is how merchants and caravans emerge.

The point where several caravan routes intersect becomes a place for a joint stopover. In this case, a more efficient exchange of both “goods” and information can take place among merchants. Moreover, merchants can agree to meet again the following season. This is how seasonal fairs emerge.

The number of fairs begins to grow. Each one develops its own set of rules. The fairs that grow the fastest are those with better conditions for trade and where clear rules of interaction—recognized by the majority—are maintained. These rules differ sharply from the rules and interactions within a traditional community. The fair organizers, above all, have a stake in upholding these new rules. And they allocate some of their resources to ensure the new rules are enforced within their territory.

The largest and most successful fairs attract merchants and representatives of other peoples. International trade brings peoples closer together, forming common rules of exchange

and a common language of exchange. Territories emerge where common rules of exchange are established. These rules no longer depend on the tribal, ethnic, or racial differences of the participants in the exchange. That is, they are formal in nature. A market emerges.

The market is a set of formal rules of exchange that exclude violence.

§2. Freedom and Law

Freedom — the ability to choose the type of human activity.

Human activity can be broadly divided into two parts: setting goals and finding the best ways to achieve them. To a large extent, the process of setting goals and finding the best ways to achieve them is shaped by a person's entire history of development and, it seems, is beyond their control.

Similarly, in the market, every entrepreneur is under pressure from established laws and prevailing prices and seems to have no influence over anything. It appears that their freedom is severely limited.

In reality, it is precisely the formal laws of the market—which do not depend on any specific entrepreneur—that grant them freedom, that is, the opportunity to choose a type of human activity from among a greater number of established activities.

Having chosen a specific type of activity and exercised their *freedom*, the entrepreneur must decide exactly how to carry out this activity. They must decide which rules to follow and which rules to apply. They can choose those that have

already been established, or they can take a risk and create new rules on their own.

The right is the ability to choose the rules governing human activity.

Restricting or regulating this right by external forces cannot be justified in any way, since no one knows in advance which specific rules will lead to the certain achievement of the goal.

Let's consider models that illustrate these statements.

1. Soccer. Here, a person can choose what role to play. They can become a goalkeeper, a forward, a defender, a coach, a doctor, a referee, and so on. Every role within soccer is already clearly defined.

A soccer player on the field operates within a limited number of formal restrictions, which are, in essence, nothing other than the laws of soccer. It would never occur to a soccer player to change these laws. After all, that would alter the game he himself chose.

The rules are considered to be immutable, having always existed and never subject to change. A thorough understanding of the rules and the development of the ability to follow them automatically (literacy) gives the player the freedom to choose how to act on the field. A player who does not know the rules well or has not developed the skill to automatically follow them is forced to spend most of their time and energy coordinating their actions with these rules. But this limits only the effectiveness of their play, not their freedom.

Thus, the laws of soccer do not infringe upon the player's freedom. First, no one restricts his desire to play. Second, the player voluntarily agreed to follow the rules; no one forced him to play soccer specifically. Third, the player

always has the option to leave the game. And fourth, it is precisely the skill of adhering to the rules of soccer that gives the player the ability to choose courses of action on the field and shapes his freedom.

How exactly (within the rules of soccer) to play is decided by the player himself. That is his right.

Exactly how (within the framework of soccer) and according to which rules to train the team is decided by the coach himself. That is his right.

Why do people play soccer? There are two main goals: to earn money and to have fun.

Professional players participate in the game to earn money. And it is easier for them to accept the existing rules and conditions of the game and offer their services to team owners than to create a team themselves or develop a new game with new rules. That is, it is easier for them to choose one of the existing types of human activity than to create a new one. The latter is too costly.

If a person plays for enjoyment, they have to pay out of their own pocket for the opportunity to participate in the game. The ball and the field cost money. But even here, it is easier for the player to play by the rules everyone knows than to develop their own rules and introduce them to others.

In both cases, “too costly” does not mean that no one will be willing to bear these costs. After all, if successful, both the profit and the pleasure gained will be orders of magnitude greater.

2. Chess. It is clear that a chess player’s choice of move is determined by the rules of the game. A chess player cannot influence these rules. But within the framework of this game,

there are an infinite number of possible moves. The chess player has a choice.

The choice of a specific move is also determined by the chess player's entire prior development: their teachers, their experience, their knowledge—and yet, it seems, it does not depend on them. But even within these parameters, there are many possible courses of action. The chess player can make their own choice. That is their *right*.

To independently choose a course of action, analysis is required: what we have, what we want to have, and how to move from the current state to the desired one. And analysis is possible only if all events are interconnected.

On the chessboard, all events are bound by a single set of rules. Moreover, these connections are always unambiguous. A limited number of formal restrictions imposed on the movement and action of each piece creates the possibility of constructing countless options for action—combinations that can lead to the desired result.

A chess player can create their own unique combination, and that is their choice. If successful, that combination becomes well-known and adopted by everyone.

Similarly, in the market, it is easier for an entrepreneur to fit into the existing system of rules than to invent new ones.

When comparing prices for goods, it is easier for an entrepreneur to accept established prices than to conduct independent research on supply and demand. The latter is too costly.

But this does not mean that there will be no entrepreneurs willing to incur the additional costs of studying supply and demand. After all, if they succeed and obtain more

accurate information about prices, the profit from the transaction will be much higher.

Thus, the market, like soccer or chess, consists of a limited number of formal prohibitions and laws. A person has the ability to choose a type of activity—that is, *freedom*—and the ability to choose how to conduct that activity—that is, *a right*.

§3. Value and Price

If, over a long period of time, the exchange “2 axes = 1 hat” occurs regularly in a given territory, then people say “two axes are worth one hat” or “one hat is worth two axes.” The economic term “value” most likely arose from a literal comparison of goods placed on the same table. That is, one party places a hat on the table, and the other places an axe. If the exchange takes place, these goods were placed (stood) opposite each other. This value becomes customary (normal), and in the next exchange, this ratio will most likely be maintained. They say the value has been established. Thus, *value* is the quantity of one good allocated in exchange for a given good.

Price is the value of a single unit of a good.

Established prices are difficult to change, because in this case, the person changing them will be perceived as someone going against custom and public opinion. They will lose their reputation. Reputation is also a commodity.

Deciding to lose one’s reputation for the sake of changing the established value of “2 axes = 1 hat” is not profitable. To take this step, one needs compelling justifications that are understandable to everyone.

On the other hand, established prices not only save time spent on bargaining but also allow one to calculate the possible outcomes of a transaction in advance. That is, established prices allow one to build models of possible actions and decide in advance which of these models will be realized in practice. This is *economic calculation*.

§4. Economic Calculation

The market allows for the establishment of relatively stable exchange ratios between goods. Prices are the most readily available information for an entrepreneur. Based on prices, he can perform economic calculations.

An entrepreneur can use established calculation models or create a new one.

It is clear that a pioneer always takes a risk. Analysis is precisely what is needed to minimize risk. And economic analysis is possible only if there are connections between events and certain patterns. For some, these connections and patterns are indistinguishable, while for others, they may become discernible.

So, there are specific entrepreneurs who incur significant costs to conduct research that reveals new price ratios. Based on the results of this research, they can develop new rules. If successful, these new rules and prices become part of the market and are available to everyone.

The market is a dynamic, evolving system. It is the result of entrepreneurs' ongoing research. But the entrepreneur himself does not set out to develop the market. He doesn't even think about it. He thinks only of his own profit. Yet it is precisely this activity that leads to unintended consequences:

the development of the market. If entrepreneurs were to deliberately set out to develop the market, the market would most likely disappear.

The market is a system of spontaneously emerging rules of exchange. Spontaneous order can arise only in open systems. The market allows people to successfully solve many problems. That is why one often hears the expression “the market will solve everything.” It is not the market that solves problems. It is the active individual who solves them. The market is merely a set of rules that create the conditions for human activity.

§5. Competition

Market laws are a set of formal prohibitions (rules). They establish what cannot be done—that is, prohibitions. Above all, violence cannot be used.

And what can and should be done?

Market forces do not dictate this.

Each market participant decides for themselves exactly what to do and how to do it.

An entrepreneur has direct access to only a very small fraction of information about available resources and their availability or scarcity. Typically, they know only what belongs directly to them and what is available in a small area around them. But market prices provide, albeit indirectly, fairly comprehensive information about resources and their availability in various parts of the world.

If a resource that is quite rare in this area appears on the market, it means there is a place where it is available in sufficient quantities and prices there are quite low. This means

an entrepreneur has discovered this resource and was able to bring it to the local market, where it costs much more than where it was found.

If asked why he is selling this resource at a price higher than what he paid for it, the entrepreneur might quite reasonably suggest that the questioner go and get the goods himself. After all, one could argue that the entrepreneur is selling his goods for the same price he paid, and the markup is payment for the services of discovering and delivering them.

Nevertheless, over time, information about the availability of a resource somewhere at a lower price becomes accessible to other entrepreneurs. There will always be a sufficient number of enterprising people who want to follow in the pioneer's footsteps. Clearly, this will lead to an increase in the supply of this product in the local market. Its price will begin to fall. In other words, the profit margin for delivering the product will start to shrink. *Competition* will arise among suppliers, which will weed out the best ones in the market. The best ones will remain. And those whose delivery costs begin to exceed their sales revenue will be forced to pursue another line of business, one in which they might be more successful.

The same applies to production. The invention or discovery of a new production technology will reduce the costs of "delivering" goods. With stable market prices, this means increased profits. The new technology allows for an increase in the supply of this good on the market. As long as there is only one innovator, this increase in supply is insignificant and does not lead to a noticeable decrease in the price of this good.

But the newly discovered technology soon becomes available to other entrepreneurs as well. They, too, begin to apply it, which leads to a significant increase in the quantity of goods produced and, consequently, to a drop in their prices.

Competition among entrepreneurs intensifies, and only the best remain in the market. Those whose production costs begin to exceed sales revenue will be forced to pursue other ventures in which they may be more successful.

Competition allows for identifying the best fulfillers of consumer desires. Specifically, consumers, since in a free market, they alone are the judges. By voting with their rubles, they determine who, from their perspective, are the best fulfillers of their desires.

But competition does more than just help identify the best performers. Entrepreneurs seeking to increase their profits are constantly on the lookout for new solutions. In other words, competition enables the creation of entirely new products and services.

Competition — a contest among entrepreneurs for consumers' money.

At the same time, some competing entrepreneurs may not even be aware of each other's existence. Competition precludes direct influence by competing parties on one another. Each competing party attempts to shape the perception of the consumer—and only the consumer—regarding the goods or services they offer. Direct influence on a competitor is prohibited by market laws.

§6. Monopoly

A situation may arise in the market where a single entrepreneur owns a specific type of resource. An entrepreneur who is the sole owner of a given type of good or service is called *a monopolist*.

A monopoly is the sole ownership of a scarce resource.

Suppose a certain entrepreneur has become the sole owner of all copper mines or the owner of the only railroad. In these cases, he will be called a monopolist. At first glance, it may seem that there is no competition here, and the monopolist can arbitrarily dictate prices for his exclusive good or service. But this is only at first glance.

The entrepreneur's goal is not simply to raise prices. The entrepreneur adjusts the price charged for their product with the aim of maximizing *profit*. And maximum profit is not achieved simply by raising the price. After all, when the price rises above a certain critical level, the number of buyers begins to fall, which leads to a decrease in profit. In the extreme, at a very high price, profit may even be zero.

A monopolist's main goal is the same as that of all entrepreneurs—to maximize profit.

If the owner of the only copper mine begins to lower the prices of the copper sold, this will lead to an increase in sales. The quantity of copper sold will increase, but so will the total costs associated with “delivering” the copper to the consumer. Moreover, the production costs per unit of copper remain the same. A decrease in the price per unit of copper sold will lead to a decrease in profit; that is, the profit may even become negative. In other words, losses will occur.

If the price of copper increases, some buyers will switch to using other metals, while others will shut down their copper-related businesses entirely.

Since costs have already been incurred to “deliver” the copper, a sharp drop in sales volume—even with high revenue per individual sale—could cause overall profit to start declining. Once again, the specter of losses begins to loom.

Consequently, a monopolist, just like any other entrepreneur, is forced to set not simply the highest possible price, but the price at which profit will be maximized. After all, the monopolist has competitors: first, producers of other types of metals; and second, the buyers themselves, who may simply choose not to purchase.

The same applies to railways. If transportation service prices are low, the costs of maintaining the tracks may not be covered by the revenue from their use. If prices are excessively high, the number of users will begin to drop sharply. After all, there are other roads and other modes of transportation besides the railway. Some customers will prefer those alternatives. And some customers may decide not to travel at all. Profits will begin to decline again.

Thus, a monopolist, just like any other entrepreneur, cannot simply set a high price. They are forced to find the optimal price at which profits will be maximized. In other words, the competition for consumers' money continues, which means that competition does exist.

Every entrepreneur, in pursuit of maximum profit, is compelled to find conditions under which this scarce resource would be allocated to the maximum number of users at the highest possible price. As a result, this scarce resource ends up in the hands of the most efficient users. That is, the condition of optimal use of this scarce resource—from the standpoint of social necessity—is met.

No research institute, no matter how many brilliant specialists it employs or how powerful its technical resources are, could physically perform such work or solve this equation. This equation has too many constantly changing variables, including the human factor.

Such equations are solved only by the activities of entrepreneurs in a free market. Moreover, the entrepreneurs

themselves did not set out to optimize the use of scarce resources for society at all. They set out only to optimize their own profits. But it turns out that it is precisely the pursuit of profit within the framework of market laws that leads to an unintended result—the most efficient use of scarce resources to meet the needs of society as a whole.

CHAPTER 7. DIVISION OF LABOR

§1. Labor

In the earliest times, humans, like animals, obtained the resources necessary for life through gathering or hunting. Over time, using their ability to think abstractly and reason, humans learned to produce the resources they needed. This is a new method.

Human activity aimed at developing new ways of acquiring goods is called labor.

The results of different people's activities, for quite understandable reasons, vary quite significantly. After all, people's physical and intellectual abilities differ.

At the same time, skills and abilities also depend on the territory where people live. Residents of coastal areas have certain skills, while those of the mountains or forests have others. Thus, regions naturally emerge where tribal groups specialize in a particular type of activity. A *division* of labor takes place. As already noted, trade begins between these tribes. Moreover, this trade involves not only local natural resources but also agricultural products and handicrafts.

A division of labor also occurs within tribal communities. Individual clans and families specialize in specific types of activity. Skills are passed down from generation to generation.

The refinement of tools and the increase in their number began to distinguish individual specialists who performed this work better and faster than others. Professions emerged. But for the time being, the entire process of producing handicrafts remained under the control of the individual specialist. A shoemaker, for example, performed all the work necessary to make a boot from available resources—he labored.

The growth of trade and specialization in the production of goods led to the emergence of permanent, protected trade centers where artisans settled. Cities began to appear.

As cities grew and population density increased, there was a greater demand for consumer goods. Consequently, the volume of goods purchased by merchant traders grew. Naturally, there were entrepreneurs who saw an opportunity in this. To increase labor productivity, *the division* of labor began to be practiced. A skilled craftsman delegated part of his work to a hired worker, training him in the relevant tasks. A new social group emerged—wage laborers. Thus, a distinction must be made between labor and work.

Bringing individual specialists together into groups allowed for the production and accumulation of larger quantities of goods in one place for wholesale sale. Such associations came to be known as *guilds*.

In medieval cities, we see the emergence of a large number of different guild associations. Activities within each guild were strictly regulated.

Mastering a skill required the constant and repeated performance of the same procedure, bringing it to the necessary level of automaticity. Consequently, the procedures

themselves, for the successful training of novices, had to remain unchanged. The statutes of some guilds remained unchanged for centuries.

The division of labor and trade significantly raised the standard of living in cities. Quality of life and life expectancy continued to rise. The population also grew. This led to even greater demand for consumer goods. Merchants were willing to purchase far more goods than the guilds could produce. And, of course, entrepreneurs reappeared who saw an opportunity for increased profits in this.

But how could labor productivity be increased?

Traditional workshops, with their inflexible rules, lagged behind market demands.

Some entrepreneurs discovered that breaking down the manufacturing process for a specific product into many small, separate operations could solve the problem of finding a large number of skilled specialists. It is much easier to teach a novice to perform a single simple operation than to train them to make the entire product. True, the number of workers needed to complete the full production cycle increased many times over. Whereas previously one boot was made by one shoemaker, now one boot is made by five or six people. But if successful, the daily output was also expected to increase significantly. The risk was well worth it. And those who took the risk did not lose out. The division of labor continued to develop.

In fact, the division of labor made it possible to increase the quantity and quality of manufactured goods many times over. Entrepreneurs began to build large factories, in which the manufacturing process was broken down into many small sequential operations that did not require high

qualifications to perform. Since the majority of the adult urban population was employed in craft guilds, the shortage of labor in factories began to be filled by children or migrants from the countryside. Special dormitories were even built for the latter. The profits earned by factory owners made this possible. Moreover, the wages paid to children in factories soon equaled those of artisans in workshops.

On the other hand, the workshops themselves began to suffer losses. Their goods proved too expensive compared to those manufactured in factories. Soon, the children's places in the factories were taken by their parents.

David Ricardo succeeded in mathematically describing the phenomenon of a manifold increase in productivity through the division of labor. This description was called the law of the formation of human connections.

§2. The Law of the Formation of Human Connections

Let us consider several cases in sequence.

1. Two craftsmen make hats. The first makes five hats a day, while the second makes only two. Is it possible for them to form a partnership here? Would it be profitable for them to join forces in a single workshop?

Most likely not. There is no division of labor here; only hats are produced. Merging would not benefit anyone. Merging would not increase the number of hats produced. The craftsmen remain competitors.

2. The same two craftsmen make hats and gloves. The first craftsman makes 4 hats in the first half of the day and 6 pairs of gloves in the second half. The second craftsman

makes 2 hats in the first half of the day and 8 pairs of gloves in the second half. Is cooperation possible here? Are synergies formed here?

A division of labor is possible here. But will it bring greater profit to both?

So, working separately, they produce a total of 6 hats and 14 pairs of gloves in a day. That's 20 items in total.

If they join forces, the first craftsman can focus solely on making hats, and the second on making gloves. Now each does what they do best.

In this case, the first craftsman will make 8 hats per day, and the second craftsman will make 16 pairs of gloves. That adds up to 24 items.

Here, cooperation is possible. It is beneficial.

3. Let's consider a case where the second craftsman makes fewer hats and gloves per day than the first.

Suppose the first craftsman makes 4 hats in the first half of the day and 8 pairs of gloves in the second half. And the second craftsman makes 2 hats in the first half of the day and 4 pairs of gloves in the second half. Is cooperation possible here? Are there any synergies here?

Working separately, they will make a total of 6 hats and 12 pairs of gloves. That is 18 units of goods.

If they team up, with the first making only hats and the second only gloves, the first will make 8 hats in a day, and the second 8 pairs of gloves. That's a total of 16 units of goods. There seems to be no benefit.

But if the first person makes only gloves and the second only hats, the first will make 16 pairs of gloves a day, and the second will make 4 hats. That's a total of 20 items. That's already more than if they worked separately.

But there is another possible scenario here. If the first person makes 4 hats and 2 pairs of gloves per day, and the second makes 2 hats and 4 pairs of gloves, then in any case the total number of goods produced remains the same. It will be constant and equal to 12. And there seems to be no point in joining forces.

Since the goods are different, they most likely have different market prices. If, for example, a single hat costs more than a pair of gloves on the market, the situation changes.

Let's say one hat costs \$10 on the market, and a pair of gloves costs \$5.

If each craftsman works separately, the first craftsman will earn \$50 for his 4 hats and 2 pairs of gloves.

The second, for their 2 hats and 4 pairs of gloves, will earn \$40.

The total revenue from the goods sold will be \$90.

However, if they collaborate and divide the labor, the first artisan can focus on making the more expensive goods. After all, that's what he does best. Now he can make 8 hats in a day. The second artisan will make only 8 pairs of gloves. But the revenue will be higher: $\$80 + \$40 = \$120$

Thus, the division of labor benefits both parties. Moreover, the one who does both jobs well will still prefer to cooperate with the one who does both worse. After all, it is to his advantage.

The division of labor softens attitudes and turns yesterday's rivals into friends.

Thus, every step toward greater division of labor benefits all participants. The division of labor expands and strengthens human connections.

Conclusion. The division and distribution of labor in a free market not only increase the total amount of goods produced, but also soften manners and strengthen bonds between people.

CHAPTER 8. CATALACTICS

To obtain a desired good, a person may set aside a portion of their existing goods—i.e., property—for exchange.

*Property set aside for exchange is called a commodity.
The part of economic theory that describes exchange is called catalactics.*

It is said that if a person has made an exchange, it means they agreed to it.¹ Otherwise, the exchange would not have taken place.

In addition, let us note that people engaging in exchange must possess property, i.e., they must be sufficiently free individuals. Thus, exchange, as we understand it today, is a relatively recent invention.

Within traditional communal groups with a subsistence economy, trade cannot arise. There is no private property here—everything is communal. The distribution of goods from the communal storehouse takes place within the framework of established traditions.

But, as we have already noted, the emergence of merchants and caravans—that is, people specifically designated by the community and equipped with specially allocated “goods”—changes the situation. Until the merchant returns to the community, he acts as the owner of the “goods.”

An encounter between a caravan and another community or another caravan gives rise to a new form of

¹ Here, we are considering a model in which violence is excluded.

exchange—trade. The exchange involves people who are independent of one another, unbound by any blood ties or other bonds. Moreover, after the exchange takes place, they may never meet again. Clearly, the exchange of stolen goods is possible here. That is why, even in the Code of Hammurabi, the death penalty was prescribed for an exchange without a witness.

Let us identify the cases in which an exchange can take place.

Generally, two people will exchange goods only if each of them considers the exchange to be beneficial to themselves.

Each party involved in the exchange has their own assessment of the goods being exchanged. At the initial stage, these assessments are compared. In other words, bargaining begins.

Barter

Let's consider the simplest case of exchange. Suppose there is already property and there is already an owner who can dispose of this property at their discretion.

Suppose one person needs an axe. In exchange, they can offer a hat. And suppose there is another person who needs a hat and who, in exchange, can offer an axe. If these two people meet, the exchange will most likely take place. After all, each of them will consider the exchange beneficial for themselves. But this does not mean at all that the exchange will necessarily take place. During the conversation these two might quarrel, and the exchange will fall through.

Therefore, let us clarify that the probability of an exchange is very high.

Since a careless word can ruin a profitable deal, trade gradually softens manners and fosters goodwill.

Each party evaluates these goods in its own way. But once the exchange is made, it is said that the value of one axe is equal to the value of one hat. Moreover, this value is now the same for both parties, even though each party's assessment of each good still differs.

A direct exchange of goods is called barter

It should be noted that what is described above is only a simplified model of a situation that may never have actually occurred. It is like the ideal gas model in physics. An ideal gas does not exist. But the gas model allows for quantitative analysis, and the results of that analysis can be applied to the study of real gas.

As we have already mentioned, in closed groups, such as a family or clan, natural exchange and trade do not exist. In these groups, the distribution of resources occurs within the framework of established traditions. Moreover, gift-giving or debt may serve as additional factors.

The first acts of exchange between representatives of two unrelated systems—that is, the first acts of breaking down closed systems—may have been quite specific. We will leave their analysis to ethnographers and historians.

Indirect exchange. Trade.

Let's complicate the previous example. Suppose the second person can offer a hat in exchange, but he doesn't

need an axe. Let's say he needs a sack of flour. Clearly, in this case, the exchange will not take place. The second party will consider the exchange unprofitable for himself.

Let's introduce a third party: a person who has a sack of flour and wants a hat in exchange. If all three meet, the exchange will most likely take place. But in this case, one of them will first have to exchange their goods for another good they don't need. For example, the first person will first exchange his hat for flour, which he himself does not need. But he knows that he can exchange the flour he received for the axe he desires. In this case, the first person has made an indirect exchange.

Indirect exchange is called trade.

Since the rules and patterns here are constant, anyone can construct and analyze a wide variety of exchange models. In doing so, the result of the analysis will be the same for everyone.

It's important to remember that in our model, all three people are complete strangers to one another. If they were members of the same tribe or clan, there would be no exchange, as we understand it. If one person—who is better at making hats—needs an axe, he'll go to his neighbor, who is better at making axes, and casually compliment the axe he likes. The neighbor would be compelled to give him the axe. After all, we're all family. If the axe owner later needs a hat, he'll visit and compliment the hat. The hat maker will have to give it to him, since he's still in his debt.

Money .

In the previous case, all three strangers met by happy coincidence. But this is a rather rare occurrence. In reality, the chain of indirect exchanges can turn out to be quite long, and finding actual agents for indirect exchange is quite difficult. Here, a certain good gradually emerges, in exchange for which most agents of exchange will agree to exchange their specific good. This selected good will be used by everyone for indirect exchange. In this case, the number of exchanges is reduced to two: 1) the available good — for the intermediary good; 2) the intermediary good — for the desired good.

How is a good identified and singled out that can serve as an intermediary in indirect exchange?

Could people simply agree on an intermediary good? Most likely not.

First, everyone has their own evaluative judgments. Second, there are too many participants in the exchange. Third, it is impossible to gather all participants in the exchange in one place and reach an agreement.

Nevertheless, such a good is identified fairly quickly, and everyone becomes aware of it and agrees on it. How does this happen?

At different times and among different peoples, a single commodity turns out to be the most in demand. The greatest demand implies the greatest exchangeability (liquidity, turnover). In the early stages, the most significant goods became such commodities. In agricultural cultures, this was grain, and in pastoral cultures, livestock. It was precisely these two types of goods that initially played the role of intermediary commodities. Or rather, the measure of these goods.

Money is a commodity with high exchangeability.

For people to accept an intermediary commodity, they must already have experience using something similar.

Many ancient written sources are actually promissory notes. Moreover, these notes could be passed from client to client and serve as an intermediary commodity. That is, a clay tablet or a split reed stick with notches could be passed along as payment for goods. This is convenient. The guarantee of receiving payment on the receipt was that everyone knew the debtor, and the relevant marks identifying the debtor and his debt were on the receipts themselves.

As trade expanded and merchant caravans traveled to distant foreign lands, this system ceased to function. But awareness of its convenience had already taken hold. In a sense, the search for a substitute for the function of promissory notes began.

As the population has grown and new social groups have emerged, the issue of identifying membership in a particular social group and distinguishing between them has become increasingly relevant. New linguistic categories emerge to distinguish these new groups, designate them, and shape specific ways of addressing them. At the same time, distinguishing objects appear. These objects determine membership in the corresponding social group. Each group has its own totemic symbol. We will refer to these distinguishing objects as distinguishing signs.

Distinguishing signs had to possess specific properties: durability and resistance to forgery or fabrication. That is, distinguishing signs were made from rather rare—and therefore expensive—materials. Later, they came to be called ornaments. In reality, of course, the point was not beauty, but

rather indicating membership in a specific social class and one's status within that class. For example, "ornaments" could be used to distinguish between unmarried and married women.

Distinctive symbols also became a means of protection. An attack on the bearer of a distinctive symbol was less likely. After all, it was known that if the bearer were attacked, their entire social group would come to their defense.

The higher the status, the more people there were who wanted to mimic the bearer of that status. Even wearing a counterfeit distinguishing mark allowed one to come under the group's protection. To reduce the possibility of forgery, distinguishing marks had to be complex to manufacture and sufficiently rare.

Initially, items of clothing served as insignia: a tall bearskin hat, a sable fur coat, gold or silver clasps and pins, and precious stones.

Later—with the collapse of tribal society and the emergence of cities—distinctive marks began to appear among private individuals (a personal stamp on goods). Consequently, promissory notes adopted a uniform standard, differing only in the owner's stamp. This became the basis for the formation of a universal medium of exchange—money in the form of coins. In the initial stage, money was purely private in nature.

Prices and Bargaining

The expansion of indirect exchange (trade) made it possible to offer, for a fee, services that closed the chain of

indirect exchanges and reduced their number. Entrepreneurs offering such services came to be known as *merchants*.

Merchants began to stockpile goods for indirect exchange in their warehouses. As the quantity of goods in warehouses increased, there arose a need to quickly determine the relative value of each good to simplify the exchange process.

The value of a unit of a given good, expressed in units of another good, came to be called a price.

It is clear that before long, price began to be determined by comparing a unit of a given good with an intermediary good—money.

When making an exchange, the presence of money was not always necessary. At fairs, when exchanging one commodity for another, their prices—expressed in money—were simply compared to quickly calculate the ratio of the quantities of the commodities being exchanged.

Traders who traveled to distant lands to procure goods came to be called *merchants*. They transported goods to other countries that were in demand there, and brought back goods that were in demand in their homeland. And trade transactions were concluded in conventional monetary units.

For example. At a fair in a particular settlement, a merchant would exchange his goods for local goods, comparing them to a known measure of grain or head of livestock, and later—to a measure of gold or silver. That is, he would first sell his goods to a local merchant, for example, for fifty measures of silver. But then, he would buy local goods from the local merchant for fifty measures of silver as well. The actual silver itself was not required. This eliminated the need to carry goods—gold and silver, which were the

primary targets of robbers—along rather dangerous roads. A measure of silver or gold served here as virtual money. Over time, a standard measure of silver emerged.

At such fairs, we identified two stages. In the first, one person offers goods to another in exchange for money. In this case, he is called *the seller*. The person who wishes to purchase these goods for money is called *the buyer*. In the second stage, they switch roles: the seller becomes the buyer, and the buyer becomes the seller.

The seller sets the price of their product based on the minimum amount of money they are willing to receive (), plus the additional amount they would like to receive.

The buyer, on the other hand, sets the price of the item they are purchasing based on the maximum amount of money they are willing to pay, minus the amount they would like to save from that sum.

For example, a merchant is willing to sell an axe for 12 silver coins. He will not accept less. But he wants to receive more and sets the price for the axe at 18 coins.

The buyer is willing to purchase the axe for 20 pieces. He will not agree to pay more. But he wishes to keep, say, 6 pieces and offers a price of 14 pieces.

As a result of the bargaining, the price may settle at, for example, 16 pieces. This amount satisfies both parties, since both will consider the exchange profitable. The seller was willing to part with the axe for 12 pieces but received 16. The buyer was willing to pay 20 pieces for the axe but paid only 16.

If the buyer agrees to pay 18 coins without bargaining, the seller will consider that the initial asking price was set too low. After the exchange, the seller will view it as

unprofitable. After all, the buyer did not bargain, meaning the seller could have set the initial price at 22 coins and received at least 20.

If the seller agrees without haggling to sell the axe for 14 coins right away, the buyer will consider their initial price to have been a mistake. After all, the seller didn't haggle, which means they could have offered 10 coins for the axe and gotten it for at least 12.

At such fairs, bargaining is a prerequisite for making a purchase. Otherwise, both parties would feel they had missed out on a bargain.

Thus, the price is usually set within the range between the seller's highest demand and the buyer's lowest offer. At the same time, the silver itself was not required. The measure of silver, which had replaced the measure of grain or livestock, continued to serve as virtual money.

In modern supermarkets, we don't see overt haggling. Each item has a price tag with a fixed price. The customer is forced to either accept the price and take the item, or refuse to pay it and walk away. Bargaining with the cashier is impossible, since prices are set not by the cashier but by the store owner. Nevertheless, bargaining does exist here as well, only in an implicit form.

Marketing

The store owner, analyzing sales trends, notices that certain items are hardly selling at all. He is forced to either remove them from the shelves and replace them with new items, or lower their price.

Conversely, the store owner notices that some items are selling out very quickly, i.e., they are flying off the shelves. He then decides to increase their stock or raise their price. These processes occur when there are a large number of purchases made by a large number of customers.

The analysis of a large number of commercial transactions, which allows one to draw conclusions about the demand for a product, is called marketing.

Transaction Costs

To exchange one good for another, it is not enough to agree on their quantitative ratios. Often, the exchange procedure itself also involves certain costs. If you have agreed to exchange 100 hats for 100 axes, the question of who should deliver their goods to whom becomes quite important. After all, transportation also costs money.

The additional costs required to complete the transaction are called transaction costs.

In fact, let's assume that you are willing to give up your axe for no less than 10 shares of silver, and are willing to take one hat for no more than 10 shares. Let's assume that the owner of the hat also values it at no less than 10 shares and is willing to give no more than 10 shares for your axe. Is an exchange possible here?

At first glance, since the owners' valuations of both goods coincide, it seems that an exchange is possible. But in reality, the exchange process itself will also incur some costs. One of the participants must transport their goods to the other,

and this will alter the price ratio, making the exchange no longer profitable for them.

Coins and Banks

Coin

Land belonging to a community (or its chief) at the intersection of trade routes, where seasonal fairs are held, is leased by other communities (or their chiefs) to establish first warehouses, then workshops, and finally a fenced-off and protected trading area (market). Later, the land tenants themselves began to sublease market stalls to merchants. Rent was calculated on a daily basis. As the market grew and the number of stalls increased, it became necessary to keep track of rent payments. Each merchant, after paying the daily rent in kind, received a token—a label certifying payment. The forms of these labels could vary across different markets. It could be, for example, a piece of leather bearing the imprint of the landlord's coat of arms or family emblem (tamga).

As trade volume increased, the short lifespan and vulnerability of the tag to forgery prompted the next step. The landlord's clan mark began to be stamped onto more durable materials. These materials could include copper, bronze, silver, or gold. Initially, the mark was applied to the coin during the casting process. This resulted in the first cast coin, one side of which bore a relief of the owner's family mark. Thus, durability and some protection against counterfeiting were achieved. But how could coins be reused? How could coins be

returned from the merchant back to the owner? If questions are asked, answers will be found.

A special building was designated as a treasury (Turkic: *khazna*), where payments in kind were accepted for the daily rent of a market stall. A coin was issued in exchange for the goods received. Special inspectors would make their rounds through the market every day at a set time, no longer issuing coins but collecting them back. If a coin was not presented, the stall would be closed until the owner went to the cashier and purchased a coin certifying payment. The absence of a coin could also serve as grounds for imposing a fine.

Thus, the coins issued at the cash register were returned to the same cash register.

Buyers paid nothing for access to the market. There was a separate entrance for them, called the “needle’s eye” (due to its resemblance to the shape of the end of the thread holder on old needles). Only people could physically pass through it; pack animals could not.

Since many merchants rented stalls for long periods, they might have dozens of coins on hand—as a sign of bulk payment for dozens of days.

A merchant might end his trading season early. In that case, he could save the remaining coins for the next season or sell them to neighboring merchants, of course, at a lower price.

A merchant who had several coins on hand for several prepaid days could sell a coin to a neighboring merchant if the latter’s time to pay the inspectors had come and he had no coins. In this case, the coin’s value increased.

Thus, within this market, the coin gradually became a means of payment between the merchants themselves and the buyers. The landlord who minted the coins could not help but

notice this. He began to use the “cash register” not only to collect payments for market stalls but also to issue coins on credit. This additional financial mechanism unexpectedly began to generate significant profits. After all, the participants in commercial transactions who used coins noticed how much the very process of trading, planning, and economic calculation had been simplified, and they now required more and more coins.

Cast coins are durable, but they are easy to counterfeit. Casting was replaced by minting—the process of stamping an image onto the coin. Initially, coins were minted on only one side. Coins with a single-sided stamp were called bracteates (Latin *bractea*—sheet metal). Later, they were minted on both sides.

In many countries, the silver coin used to pay the daily fee for a standard trading spot was called a “tanga” or “denga,” derived from the word “tamga”—a clan mark.

The increase in silver coin production led to a rise in the price of silver. This, in turn, led to the practice of debasing coins, i.e., scraping off a small amount of silver from the coin. This altered the coin’s weight—and thus its value—which led to disputes during transactions and eroded trust in the currency.

The owner who minted the coins was forced to bear additional costs for identifying and sending damaged and counterfeit coins to be melted down. To solve this problem, it was necessary to assemble and train a special team.

After some time, the owner who minted and put the coins into circulation noticed that coins could be exchanged for any goods at the market. This allowed for a change in the payment system at the cash register. Now, instead of food (goods), coins themselves were required as payment for a

market stall. Coins could only be purchased at the market or at the same cash register, but only on credit. The cash register began to take on the characteristics of a future bank.

If, in a given market, the introduction of a coinage system simplified payments (trade) and gave rise to a new financial mechanism that allowed the owner of the mint to reap substantial profits, this could not have gone unnoticed in other markets. Consequently, it could have happened that a merchant arriving from another market might have tried to buy goods in this market using coins obtained in another market. But the coins could differ in both weight and the markings on them. At first, there was no trust in coins from other markets in this market, and they were not accepted. But the cashier could not help but notice the profit to be made from exchanging coins. After all, in this case, the exchange took place at a value lower than the face value indicated by the coins' weight. The cashier's desk became a place where a new service was provided: the exchange of coins from one market for coins from another market.

The constant exchange of coins from different markets led to the standardization of coin shape and weight. At the same time, competition began among the coins. Coins of the same denomination (weight) but with different mint marks were valued differently. Some coins, whose owners took greater care to prevent their damage or counterfeiting, were treated with greater trust, while others were treated with less. The former came to be called "good money," and the latter—"bad money." In a free market, good money drives out bad money, bringing greater profits to its owners.

Seeing the profits that minting coins for retail trade brings them, coin owners strive to expand the scope of its use.

They may rent space in other markets to open branches of their cash office or exchange point there. This is how the networked banking system is born. Gradually, the term “cashier’s office” comes to refer only to a place for receiving or dispensing cash. And the building where all other operations take place—from minting to exchange and lending—is called a “bank” (Latin *banco*—a bench, counter, or table on which money changers laid out coins).

The development of retail trade made it possible to establish permanent markets in place of seasonal fairs. After all, there were now no problems with food supply. Agricultural producers themselves brought their products to the permanent fairs with the intention of exchanging them for coins, and then using those coins to buy necessary goods at the market. A city emerges. The emergence of the city also changes the structure of the patriarchal-communal system, giving rise to landowners—Cossacks or farmers—who have separated from the community.

Thus, two new concepts—the bank and the coin—radically transformed the exchange system: the market and retail trade emerged. The banking network system made it possible to organize coin minting, monitor the quality of coins in circulation, and combat counterfeiters. It was also here that coins were exchanged and issued on credit, i.e., loans were granted.

Let’s take a closer look at some of the new functions of banks that emerged later.

Money storage and safe deposit boxes

A person who has accumulated a significant amount of coins or treasures faces the problem of storing them safely. They are willing to pay to solve this problem. Some entrepreneurs, noticing this new demand in the market, began to establish businesses for the storage and protection of such valuables.

Clearly, a specialist (banker) can solve the problem of safe storage better than the owner of the valuables. The number of the bank's clients begins to grow, providing the owner with a steady, reliable income.

The owner of the money or treasures receives a *promissory note* from the banker—a personalized receipt acknowledging their acceptance into storage. The banker knows the depositor personally and will not hand over the deposit to a stranger based on this receipt.

News of this new profitable venture spreads throughout the market. Competition among bankers begins. The price for banking services begins to fall.

Competition, as we have already mentioned, not only identifies the best specialists but also allows for the discovery of new types of services. Let's examine, using models, the evolution of banking services born of competition. It should be noted, however, that this analysis is conducted in hindsight. No one could have predicted anything like this in advance, even using models.

One banker observes that some clients would prefer not to reveal the items they are depositing for safekeeping. The banker offers the client a safe deposit box in which anything the client wishes can be stored, but only the client will know

exactly what is inside. The client simply pays for the rental of the box.

Transfer from one account to another

If a depositor needs to make a large purchase, they have to go to the bank to get their money. Leaving the bank with a large sum, they become a target for robbers. A banker, noticing that the same money is being brought in for safekeeping at his bank by another depositor that evening, realizes he can offer a new service—transferring funds from one account to another at the depositor’s request.

In fact, if depositor “A” took 1,000 gold coins from the bank to buy a house from depositor “B,” then most likely depositor “B” will bring those same 1,000 coins to the same bank for safekeeping.

The banker suggests simply transferring 1,000 coins from Account A to Account B. This is completely safe.

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Every time two bank customers come to the banker with a request to transfer money from one account to another, he realizes that the customers are wasting their time on a fairly simple transaction that could be carried out without their physical presence at the bank. He offers the customers a new type of bill—an *assignment*, i.e., a bearer bill. It differed from a registered bill of exchange in that anyone to whom the owner transferred it could present it for payment.

Now, Client A simply needs to hand Client B an assignment for 1,000 coins and make a purchase. Neither of them needs to go to the bank.

Checkbook.

The number of customers at the bank offering and accepting promissory notes begins to grow. The bank's profits also grow. But other bankers learn of this innovation. They begin to do the same—offering their own promissory notes.

One of the bankers notices that customers are forced to come to the bank to request banknotes for the specific amount of the transaction. After all, the amounts vary, and no one knows in advance what denomination might be needed. The banker offers the customer *a checkbook*—a set of pre-printed bank check forms where one only needs to fill in the amount and sign.

Now every customer can fill in the desired amount themselves, and there is no need to go to the bank.

Banknote

Banks that offer checkbooks and accept checks are seeing their customer base grow. But as word of this innovation spreads, all banks are now offering their own checkbooks to customers. For now, however, only relatively wealthy individuals use them, to pay for large purchases. They know one another and are familiar with how banks operate.

One of the bankers has a brilliant idea: it would be nice if small purchases could also be paid for with checks.

However, the banker realizes that filling out checks with various small amounts and having customers sign them would be inconvenient. He offers customers a set of checks with fixed denominations and all the necessary stamps and signatures—*banknotes*.

Now the customer can put together the necessary amount themselves by selecting banknotes of the appropriate denominations. In addition, it became possible to pay for small purchases.

At first, this innovation is met with cautious skepticism. Not everyone is willing to accept a banknote in a store instead of the usual silver or gold coins. Moreover, not everyone knows what to do with it. Spend time collecting these banknotes and heading to an unfamiliar bank to exchange them for cash (coins)? Few are willing to do that. But the shop owners who did take the plunge were pleased to discover that the number of their regular customers began to grow. Moreover, the shop owner became familiar with how the bank operates and realized that it was better to keep his revenue there and keep banknotes in his own cash register. After all, he could offer banknotes as change to a customer paying for a purchase with a banknote. And the banker immediately realizes that by opening accounts for small shopkeepers, he significantly increases the number of customers—and thus his own income.

This innovation becomes widely known. Now banknotes are accepted as payment at all retail outlets. Competition among bankers intensifies. After all, consumers prefer banknotes from specific banks. And they refuse to accept banknotes from some banks altogether.

Bank transfers

Banks with a large number of customers can now afford to open branches in other cities. This makes it possible to offer a new type of service—transferring money from a bank account in one city to an account in another city. Clearly, this frees customers from having to transport gold and silver coins along rather dangerous roads. It is enough to deposit their money at a bank in one city and receive it at its branch in another city. This innovation is becoming widely known, but not all banks have branches.

However, bankers with a branch in another city face an initial problem: a customer who presents promissory notes or banknotes for cashing may not have enough coins in their account at that branch. What should be done? They have to either refuse to pay out the money or suggest waiting until coins are brought from the other city from the customer's account. Both options are highly undesirable.

Bank Reserve

The banker finds a solution: he creates a reserve fund using his own funds. From this fund, the bank branch in question issues the missing coins to the person presenting the banknotes. The banker then recovers his money by debiting it from the customer's account at another bank.

Bankers with a reserve fund strengthen their position by increasing their customer base.

Interbank Transactions

The growth of trade between cities is driving the development of transportation and delivery services. One banker comes up with the idea of offering his clients services to pay for purchases in another city. For those bankers who have opened a branch in another city, this is easy to do. But no one is yet able to have branches in every city. However, there are other banks there with which agreements can be made. Negotiations begin among the bankers. Two bankers who have banks in different cities can agree to accept each other's banknotes for cashing. This benefits both parties.

But this raises a new problem. If a banknote from another bank is presented for redemption at a given bank, this means that coins must be issued to a customer who did not deposit them with that bank. Consequently, as in the case of branches, partner banks will be forced to maintain reserve funds to pay for each other's banknotes. Consequently, bankers will be forced to periodically conduct mutual settlements to replenish their reserve funds. Gold and silver bars began to be used for mutual settlements between banks.

Timely fulfillment of the mutual settlement agreement becomes a vital element for a banker. After all, failure to issue money in exchange for a promissory note or banknote constitutes proof of fraud on the part of that bank, i.e., its *bankruptcy*. All customers would leave such a bank. A bank's reputation becomes a decisive factor, and bankers are forced to be very cautious when entering into partnership agreements with other banks.

Banks with a strong reputation begin to generate higher profits. A banker's reputation, like that of any entrepreneur, becomes a new kind of resource.

Credit

As the number of services offered by banks increases, their customer base grows exponentially. So does the profitability of banking. Competition among bankers intensifies. They continue to seek out and discover new types of services in the market. This means they are looking for new problems whose solutions are in demand by entrepreneurs.

One banker noted that many entrepreneurs have begun using bank accounts to accumulate funds that will be used in the future to expand their businesses or start new ones.

Capital — a portion of property allocated for conducting and expanding production.

Drawing on his experience in establishing reserve funds for his branches, the banker began setting up loan funds for entrepreneurs and offering them loans.

It is advantageous for an entrepreneur to take out a loan and expand production today, and then repay that loan tomorrow using the additional profits earned.

A loan must be repaid. After all, in this way, the entrepreneur is buying time—the rarest of resources. Consequently, *loan interest* is added to the initial cost of the resource.

To obtain a loan, entrepreneurs must open an account at the bank. Moreover, the bank's specialists review each loan application quite thoroughly: they must be certain that the loan will be repaid, with interest. Here, the borrower's reputation becomes one of the most important factors.

Stock Market. Stock Exchange

Some bankers, aware of deposits that had been sitting idle in their banks' accounts for quite some time, began offering depositors the opportunity to become partners in maintaining the bank's loan reserve. In fact, a depositor who transferred part of their funds to the reserve fund could receive a share of the profits from this new business venture in the form of interest on the transferred portion. In this case, they no longer had to pay for the service of holding funds in the bank's accounts; on the contrary, they themselves received income, which came to be called *a dividend*.

To participate in the credit reserve fund, a depositor was offered the option to open a special fixed-term account, meaning the client agreed not to demand the return of their deposit from this account during the term specified in the contract. The bank would use these funds as a means of lending. In return, the depositor received a certain percentage of their term deposit each month. If, however, the depositor did demand the return of the money before the term ended, then, usually, according to the contract, they had to return all dividends received. This was advantageous for depositors.

But for the banker, this was a risky business. In the event of a loan default, he lost not only his own money but also his partners' money. After all, regardless of the outcome of his lending, the banker was obligated, at the end of the term specified in the contract, to return all funds deposited by the depositor plus interest.

Joint-Stock Company

Over time, bankers began to emerge who, in agreements on equity participation in a reserve credit fund, offered participants the right to dividends proportional to their contributions. In return, depositors agree to bear the risks. That is, in the event of loan defaults, losses are also shared among investors in proportion to their contributions. However, in this case, investors find themselves at a disadvantage. In return, they began to demand a say in key decisions regarding loan allocation. To implement these projects, a new type of enterprise had to be established—a joint-stock company. Each depositor received shares in exchange for their deposit and the right to vote at the shareholders' meeting, proportional to the number of shares held. Clearly, not all depositors understand the intricacies of lending. Therefore, at the shareholders' meeting, members of the joint-stock company's board were elected, whom the depositors trusted to manage the business. But in this case, the banker ceases to be the owner and manager of the credit fund.

In the new structure—a joint-stock company—there are new owners. These are the shareholders.

Shares are outwardly very similar to bank notes. But unlike them, the value of a share can fluctuate within a fairly wide range.

A promissory note corresponds to a very specific amount of gold or silver indicated on it. Metal prices are relatively stable.

The value of shares, however, depends on the success of the company in which the shareholders' funds were invested. If the company's revenue grows, so does the value of the shares: a percentage of the profit—a *dividend*—is

added to them. But in the event of failure, the shares may lose all their value, and the shareholder loses all the funds invested.

It was impossible to withdraw the money invested in a credit fund via shares before the specified term. After all, this would constitute a breach of the term deposit agreement.

CONCLUSION

A human being is forced, first and foremost, to worry about their physical survival. Whether alone or as part of a group, they must act to survive. This is a goal dictated by nature itself.

But humans have learned to set new goals that do not exist in nature. To achieve a goal, one must act. Action requires resources. The resources available to humans are limited. An intermediate goal emerges—the acquisition of necessary resources (goods).

We have examined the fundamental principles of economic theory, which describes the patterns and regularities of human activity aimed at allocating acquired resources among established goals. The foundation of this activity lies in thinking and communication—that is, modeling and analyzing activity through abstractions and exchanging the results of thought through language.

Human activity—the collective activity of many generations of entrepreneurs, rejecting violence and fostering cooperation—has built the modern world. The laws they discovered have become the foundation of modern civilization. Distorting these laws or disregarding them for the sake of short-term private gains could destroy this civilization.

In this guide, we have not considered forms of non-economic interference in human activity, such as theft, robbery, banditry, fraud, etc. Nor have we considered activities that create the conditions for economic activity.

Creating the conditions for economic activity and the functioning of the market is an important part of human activity. Property and profit must be protected.

Human activity aimed at building an organized defense of human rights, freedoms, and property is called *politics*.

Interaction among people in the market allows for the construction of an effective system of protection just as it allows for the construction of an effective system of production and trade. After all, protection is just as much a sought-after commodity as any other. Consequently, protection has its own value, which means that people must be willing to pay for it.

There will always be entrepreneurs who offer their services to organize protection. After all, it is a profitable business. And so, professionals in this field emerge, along with competition among them. But that is a topic for another study.

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