

HAYEK

Social Theorist of the Century

Americans love to create lists of important people, events and things. As the title of this article suggests, F. A. Hayek not only belongs on a list of the century's great social theorists but deserves to be at its apex. Although Hayek is not a household name, no other 20th century social thinker has better understood how free societies work, and none has been so vindicated by unfolding events in so many intellectual areas. As 1999 is the centenary of Hayek's birth, it's an especially opportune time to examine his ideas and their real-world impact during this century, much of which Hayek—who died in 1992—lived to see.

The 20th century has seen a single, unifying intellectual struggle play out across its decades, affecting all the earth's peoples. That struggle has been between those who wished the state to impose a centrally planned order on society and those who understood that the best order—and the only one consistent with democracy and individual freedom—is a spontaneous one that does not need imposition. Such an order flourishes only under democratically, or constitutionally, restrained

*This last year of the 20th century is also the 100th anniversary of the birth of Austrian economist Friedrich von Hayek. He and American Milton Friedman stand as perhaps the most influential free market economists of the century. Hayek's *The Road to Serfdom* and other works helped turn the world away from socialist and communist ideology.*

The Federal Reserve Bank of Dallas is proud to make available this essay about Hayek and his legacy. An excellent, fuller treatment can be found in a commemorative album compiled by John Raybould and published by the Adam Smith Institute in London.

—Bob McTeer
President
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governments that operate under the rule of law. Tens of millions of people have died in this century's wars, perished under oppressive regimes or were put to death simply because they were in the political opposition. Even those who survived have often suffered harsh economic and political deprivation. This is the most visible manifestation of the ideological struggle in which Hayek was a central participant.

The Early Years and the Great Depression

The Austro-Hungarian empire was at its zenith when Hayek was growing up in pre-World War I Vienna.

He considered his an idyllic childhood.¹ The Hayek men had typically been civil servants, but Hayek and his two brothers became university professors, and his cousin, Ludwig Wittgenstein, became a world-famous philosopher.

During the Great War that transformed Europe both geographically and ideologically, Hayek served as an artillery officer in the Austrian army. He became, in his own words, a "mild socialist," who hoped that at war's end there would be a societal reorganization and world peace. In 1918 Hayek entered the University of Vienna, where he earned two doctorates, one at age 21 in

law and the second in political economy. While at the university, he had many brilliant teachers of political economy, most notably Ludwig von Mises. Mises held an honorary professorial post but, more important, hosted the fortnightly *Privatseminar*, where gifted, rising students in economics, sociology and philosophy presented their papers and where new ideas and theories were enthusiastically discussed. For Hayek, it was the beginning of a lifelong friendship with Mises, the most prominent living member of the Austrian school of economics.² Within three years, Hayek's socialistic leanings had been redirected by Mises' persuasive arguments, which were consistently rooted in the classical liberal tradition.

Because the war's aftermath brought depression to many countries and hyperinflation to Germany (which dramatically affected Austria), Hayek and Mises cofounded an institute to study business cycles. Hayek's 1929 work *Geldtheorie und Konjunkturtheorie* (later published in English as *Monetary Theory and the Trade Cycle*) drew the attention of economists in other nations, and in 1930 he was invited to London to

The Foundation of Our Civilization

Our civilization depends, not only for its origin but also for its preservation, on what can be precisely described only as the extended order of human cooperation, an order more commonly, if somewhat misleadingly, known as capitalism. To understand our civilization, one must appreciate that the extended order resulted not from human design or intention but spontaneously: it arose from unintentionally conforming to certain traditional and largely *moral* practices, many of which men tend to dislike, whose significance they usually fail to understand, whose validity they cannot prove, and which have nonetheless fairly rapidly spread by means of an evolutionary selection—the comparative increase in population and wealth—of those groups that happened to follow them. The unwitting, reluctant, even painful adoption of these practices kept these groups together, increased their access to valuable information of all sorts, and enabled them to be “fruitful, and multiply, and replenish the earth, and subdue it” (Genesis 1:28). This process is perhaps the least appreciated facet of human evolution.

...The main point of my argument is, then, that the conflict between, on one hand, advocates of the spontaneous extended human order created by a competitive market, and on the other hand by those who demand a deliberate arrangement of human interaction by central authority based on central command over available resources is due to a factual error by the latter about how knowledge is and can be generated and utilised. As a question of fact, this conflict must be settled by scientific study. Such study shows that, by following the spontaneously generated moral traditions underlying the competitive market order (traditions which do not satisfy the canons or norms of rationality embraced by most socialists), we generate and garner greater knowledge and wealth than could ever be obtained or utilised in a centrally-directed economy whose adherents claim to process strictly in accordance with “reason.” Thus socialist aims and programmes are factually impossible to achieve or execute; they also happen, into the bargain as it were, to be logically impossible. ■

—From *The Fatal Conceit: The Errors of Socialism*, 6–7.

lecture on the Austrian theory of business cycles.³

The London Years

Hayek was invited to lecture at the London School of Economics (LSE) by Lionel Robbins, and in 1931 he gave the series of lectures that became *Prices and Production*.⁴ Although Hayek was coolly received at Cambridge, home of John Maynard Keynes’ “Cambridge Circus,” his lectures were enthusiastically applauded at the LSE, which offered him the Tooke Chair in Economic Science and Sta-

tistics the following year. Hayek promptly accepted, which led to his permanent residence, and citizenship, in Britain. Except for a brief stint at Cambridge during World War II, he remained at the LSE until 1950.

It was during Hayek’s London days that he became internationally recognized as one of the world’s leading classical liberal scholars and thinkers. *Prices and Production* was followed by *Collectivist Economic Planning*, *The Pure Theory of Capital* and the book that would introduce him to the general public on both sides

of the Atlantic, *The Road to Serfdom*. This book, completed in 1944, sold so well that the University of Chicago Press had to reprint it three times in the first three weeks after its release. The Book-of-the-Month Club distributed 600,000 copies of the condensed version, which had been serialized in *Reader’s Digest*.⁵ Ultimately, this work would become a multi-million worldwide best-seller.

Hayek was better known to the general public than even Keynes, whose policy ideas and macroeconomic theories dominated the post-war world. But Hayek’s career seemed at its peak, for after his penetrating dissection of socialism, the general academic community slowly turned chilly toward him. The Labour Party, full of avowed socialists who wanted to implement many of the policies Hayek’s book had condemned, took power in 1945. The political and intellectual climate in Hayek’s adopted country was decidedly hostile to his antisocial-

ist, antiplanning arguments. He retreated to academia and in 1948 published *Individualism and Economic Order*, a book of essays that dissented from the postwar embrace of ever-widening government intervention.

Believing the classical liberal order was under theoretical and political assault in 1947, Hayek founded an organization whose purpose was “to work out the principles which would secure the preservation of a free society” and to promote such a society internationally. The new group was named after the site of its initial meeting, Mont Pelerin on Lake Geneva, Switzerland. The first meeting of the Mont Pelerin Society drew a glittering collection of intellectuals from around the world, many of whom had never met because of wartime travel restrictions. The society would ultimately succeed in making a reality of Hayek’s vision of retaking the future from the then-dominant statist movements.⁶

The Condition of the Working Class Under Capitalism

There is, however, one supreme myth which more than any other has served to discredit the economic system to which we owe our present-day civilization...[I]t is the legend of the deterioration of the position of the working classes in consequence of the rise of “capitalism” (or of the “manufacturing” or the “industrial system”). Who has not heard of the “horrors of early capitalism” and gained the impression that the advent of this system brought untold new suffering to large classes who before were tolerably content and comfortable? The widespread emotional aversion to “capitalism” is closely connected with this belief that the undeniable growth of wealth which the competitive order has produced was purchased at the price of depressing the standard of life of the weakest elements of society;...[A] more careful examination of the facts has, however, led to a thorough refutation of this belief. ■

—From *Capitalism and the Historians*, 9–10.

Decentralized Knowledge and the Economic Planning Problem

The peculiar character of the problem of a rational economic order is determined precisely by the fact that the knowledge of the circumstances of which we must make use never exists in concentrated or integrated form but solely as the dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess. The economic problem of society is thus not merely a problem of how to allocate “given” resources—if “given” is taken to mean given to a single mind which deliberately solves the problem set by those “data.” It is rather a problem of how to secure the best use of resources known to any of the members of society, for ends whose relative importance only these individuals know. Or, to put it briefly, it is a problem of the utilization of knowledge which is not given to anyone in its totality...[I] should briefly mention the fact that the sort of knowledge with which I have been concerned is knowledge of the kind which by its nature cannot be conveyed to any central authority in statistical form. The statistics which such a central authority would have to use would have to be arrived at precisely by abstracting from minor differences between the things, by lumping together, as resources of one kind, items which differ as regards location, quality, and other particulars, in a way which may be very significant for the specific decision. ■

—From *Individualism and Economic Order*, 77–79.

Chicago and the Later Years

In 1950, Hayek accepted a professorship in social and moral science at the University of Chicago and joined the school's Committee on Social Thought. Through writing economic theory at this point, Hayek widened the scope of his writing and scholarship. He published works in political science, law, sociology, history of science, biography, history and even psychology. Hayek was rare in that he integrated his knowledge of economic theory with a theory about the generation, perception and evolution of knowledge generally and of all human evolution. It was during this period that he wrote *The Sensory Order*, *John Stuart Mill and Harriet Taylor*, *The Constitution of Liberty* and *The Counter-Revolution of Science*. He

also edited and wrote an introductory essay for *Capitalism and the Historians*.

In 1962, Hayek returned to Germany as a professor of economic policy at Albert Ludwigs Universität at Freiburg, West Germany. But ironically, even as he lived amid the German “economic miracle,” which his teaching had so influenced,⁷ Hayek's political positions seemed less fashionable than ever to many, and in 1968 he retired from the university and from active academic life. He became isolated and depressed and was routinely ignored or forgotten by those who disagreed with him. Despite this, Hayek was far from through with thinking and writing. The catalyst that regenerated the old fires came, surprisingly, in 1974 from socialist Sweden, when he and Gunnar Myrdal were awarded

the Nobel Memorial Prize in Economic Sciences.

His retirement financially secured by the prize money, Hayek returned to his unfinished work and completed the second and third volumes of *Law, Legislation and Liberty*, in which he elaborated on themes explored in *The Constitution of Liberty*. In his final book, *The Fatal Conceit: The Errors of Socialism*, published in 1988, Hayek took a powerful and logical look at why socialism had to fail. And then, empirically, all over the world that failure began to happen in ways so dramatic as to have been unimaginable just a few years earlier. The Soviet Union collapsed, the Berlin Wall fell and Germany was reunited. Even self-described socialist nations began to follow America's lead, cutting their tax rates and sometimes selling off their public business monopolies. Historical developments everywhere seemed to confirm Hayek's theories, and even his old nemesis—Keynesian economic theory—no longer dominated macroeconomic policy. Instead, it be-

came one of many macro-paradigm approaches that developed between 1950 and 1980, including monetarism, supply side economics, rational expectations and, of course, variations on Keynes' original ideas.⁸

As we move into a new century, Hayek's vision of a world of more open societies is arriving, albeit slowly in places. His was a remarkable life, and though he doubtlessly sometimes believed the flow of history ran against him, he always seemed optimally positioned to research and write on precisely the topics that would shape world events. He was a model scholar, always exceptionally polite to his intellectual adversaries, a prolific yet trenchant writer and an example of the type of person who lives by his professed ideals. And while in terms of policy his own century favored others—notably Marx, Pigou, Fischer, Keynes, Friedman and Mundell—the 21st may see an international blooming of societies based on his vision of a free—and a good—society. ■

—Robert L. Formaini
Senior Economist

On John Maynard Keynes

There were of course extraordinary gaps in his knowledge. His knowledge was aesthetically guided, with the result that he was completely ignorant of nineteenth-century economic history. Totally ignorant. He just disliked it. I had to tell him every day, not so much about economic history, but even about the earlier English economists. He knew his Marshall, but very little else...[H]e had hardly anything about international trade theory...[I] like to say, I liked Keynes and in many ways admired him, but do not think he was a good economist. ■

—From *Hayek on Hayek*, 92–93.

The Tempting Road to Serfdom

It is a revealing fact that few planners are content to say that central planning is desirable. Most of them affirm that we can no longer choose but are compelled by circumstances beyond our control to substitute planning for competition. The myth is deliberately cultivated that we are embarking on the new course not out of free will but because competition is spontaneously eliminated by technological changes which we neither can reverse nor should wish to prevent. This argument is rarely developed at any length—it is one of the assertions taken over by one writer from another until, by mere iteration, it has come to be accepted as an established fact. It is, nevertheless, devoid of foundation. The tendency toward monopoly and planning is not the result of any “objective facts” beyond our control but the product of opinions fostered and propagated for half a century until they have come to dominate our policy.

...[O]nce government has embarked upon planning for the sake of justice, it cannot refuse responsibility for anybody's fate or position. In a planned society we shall all know that we are better or worse off than others, not because of circumstances which nobody controls, and which it is impossible to foresee with certainty, but because some authority wills it. And all our efforts directed toward improving our position will have to aim...[a]t influencing in our favor the authority which has all the power. The nightmare of English nineteenth-century political thinkers, the state in which “no avenue to wealth and honor would exist save through the government,” would be realized in a completeness which they never imagined—though familiar enough in some countries which have passed to totalitarianism. ■

—From *The Road to Serfdom*, 43 and 107.

Notes

- ¹ Raybould (1998).
- ² Also known as the Viennese school, the Austrian school began with Carl Menger and has included or influenced, to a greater or lesser degree at various times, such notables as Eugen von Böhm-Bawerk, Friedrich von Wieser, Gottfried Haberler, Joseph Schumpeter, Oskar Morgenstern, Fritz Machlup, Lionel Robbins, Israel Kirzner, Wilhelm Röpke, G. L. S. Shackle, Ludwig Lachmann and Murray Rothbard.
- ³ Hayek visited London a year earlier for a monetary conference, where he first met his future lifelong intellectual opponent, John Maynard Keynes. Though friends, Hayek and Keynes agreed infrequently on economic theory and public policy issues.
- ⁴ Hayek (1967b).
- ⁵ Raybould (1998), 47.
- ⁶ Raybould (1998), 55–59.
- ⁷ Ludwig Earhard, whose “bonfire of controls” ignited the German economic reconstruction one Sunday afternoon in

the late 1940s, attended the second meeting of the Mont Pelerin Society. His chief economic advisor, Walter Eucken, was also a society member and later helped Hayek secure his position at Freiburg. Röpke, another Mont Pelerin member, had advised Earhard to abolish the Allied-imposed controls in 1948. After the controls were lifted, a long-running experiment unfolded that showed West Germany's freer economy was clearly superior to East Germany's communist one. The result was, of course, the erection of the Berlin Wall to prevent flight from communist East to capitalist West.

⁸ Keynesians now are in three subgroups: Neo-Keynesian, post-Keynesian and Post Keynesian. Each group is attempting to come to terms with the deficiencies of Keynes' *The General Theory of Employment, Interest and Money* in light of economic performance and policy problems since 1950.

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Further Reading on

Friedrich von Hayek

- Hayek, Friedrich von (1944), *The Road to Serfdom* (Chicago: University of Chicago Press).
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- (1976), *Law, Legislation and Liberty*, Volume 2 (Chicago: University of Chicago Press).
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- Steele, G. R. (1996), *The Economics of Friedrich Hayek* (New York: St. Martin's Press).

The University of Chicago Press is in the process of publishing Hayek's collected writings in 20 volumes. Seven of these are now available: 1, 3, 4, 5, 6, 9 and 10.

To learn more about the Raybould book, see the Adam Smith Institute's web site, www.adamsmith.org.uk.

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