

THE THEORY OF SPONTANEOUS ORDER AND CULTURAL EVOLUTION IN THE SOCIAL THEORY OF F.A. HAYEK

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If social phenomena showed no order except insofar as they were consciously designed, there would indeed be no room for theoretical sciences of society ... It is only insofar as some sort of order arises as a result of individual action but without being designed by any individual that a problem is raised which demands a theoretical explanation.

F.A. Hayek (1952a: 69)

If we had deliberately built, or were consciously shaping, the structure of human action, we would merely have to ask individuals why they had interacted with any particular structure. Whereas, in fact, specialised students, even after generations of effort, find it exceedingly difficult to explain such matters, and cannot agree on what are the causes or what will be the effects of particular events. The curious task of economics is to demonstrate to men how little they really know about what they imagine they can design.

F. A. Hayek (1988: 76)

I. Introduction

F.A. Hayek is perhaps the most broad ranging scholar to address economic issues since Adam Smith. His work has spanned across technical economics (1928, 1933a, 1935, 1937, 1939, 1941, 1945), philosophy of the social sciences (1943, 1952a, 1967, 1978), theoretical psychology (1952b), legal philosophy (1960, 1973, 1976, 1979a), and most recently social anthropology (1979b, 1988). Despite the diverse nature of his research, it has a common theme: How do social institutions work, through the filter of the human mind, to coordinate human affairs?

But Hayek's attempts to pursue this question come to us in scattered concentrations on various specific topics. This had led some scholars to miss the unity of his life-work. T.W. Hutchison, for example, argues that there is a fundamental dichotomy in Hayek's thought – a Hayek I, who is under the influence of Ludwig von Mises, and a Hayek II, who rejects Mises's praxeological method and embraces the methodological views of Karl Popper (Hutchison 1984: 176-232).

Bruce Caldwell (1988) counters Hutchinson's interpretation. It wasn't Hayek who became a Popperian but Popper who became Hayekian. But Caldwell also sees a major transformation in Hayek's work. Due to the interwar intellectual debate over socialist economic calculation, Hayek was transformed from primarily a technical economist concerned with equilibrium theorizing to a broad social theorist concerned with the coordination problem in society in general. His transformation, Caldwell argues, is a result of his growing disenchantment with equilibrium theorizing. While Caldwell's argument is convincing, as far as it goes, even Hayek's earliest work in technical economics can be seen as preparing the way for his later work in a non-equilibrium, process-oriented social theory. In his 1928 essay on "Intertemporal Price Equilibrium and Movements in the Value of Money," for example, Hayek points out, albeit in embryonic form, a theme which permeates his later economic and social theory writings, the role of prices as guides to economic coordination processes through time. As Hayek put it:

prices ... fulfill a particularly significant role with respect to the distribution of the individual processes through time, as the guide and regulator of all economic activity in the exchange economy. It is precisely this function which hitherto has received only brief mention in economics (1928: 71).

Early Hayek, as well as later Hayek, is concerned with the communicative function of social institutions in general, whether they are money prices within the economic system or the rules of behavior within social interaction. Exploring this communicative function is what motivates his research, the tools he employs (such as equilibrium theorizing in his early work or order analysis in his more recent writings) are judged by how well they aid our understanding of that function.

This unity is indicated by Hayek's continuing interest in certain fundamental questions about the nature of the mind. John Gray (1986) has argued that the unity in Hayek's research centers on his neo-Kantian epistemology. Gray relies on Hayek's *The Sensory Order*, which though published in 1952, was original conceived during his student days. And as Hayek says,

though my work has led me away from psychology, the basic idea then conceived has continued to occupy me; its outlines have gradually developed, and it has often proved helpful in dealing with the problems of the methods of the social sciences (1952b: v).

The research project of exploring the nature of the mind and its relation to human society does not only cover all of Hayek's work, but is part of a larger unity of a whole social scientific tradition tracing from Adam Smith to the modern Austrian school. Hayek's contribution to economics and social thought should be understood as the extension of a research program laid down by Adam Smith, Carl Menger, and specifically, Ludwig von Mises.¹ In this manner we can see the way in which Hayek's epistemology is translated into the core foundation of a theory of society.

In particular, Mises, the system builder, provided Hayek with a program for the study of the economic system and the social world. Hayek is the dissector and analyzer of that Misesian system. His work can be best understood as the continued attempt to make explicit what Mises left implicit, to refine what Mises stated explicitly, and to answer questions Mises left unanswered. As Hayek has said of Mises:

There is no single man to whom I owe more intellectually, even though he was never my teacher in the institutional sense of the word.... I am to the present moment pursuing the questions which he made me see, and that, I believe is the greatest benefit one scientist can confer on one of the next generation (1983: 17; 18).

This influence is obvious in Hayek's work on knowledge and the analysis of socialism, but these insights on knowledge dispersion and conveyance are inseparable from the rest of Hayek's work, from business cycles to the common law.² This paper will explore the unity in Hayek's project and its connection to his theoretical predecessors.

II. The Spontaneous Order Approach

Hayek's social theory project is the advancement and refinement of a tradition of social analysis that dates back to the Scottish Enlightenment and thinkers such as David Hume and Adam Smith. Hayek develops that tradition, however, in his own unique way by interpreting it in light of the economic and social theory tradition handed down to him via his intellectual mentors in the Austrian school of economics, Carl Menger and Ludwig von Mises. It is his Austrian perspective toward economic analysis that leads him to question the

ability of modernist economics to understand spontaneously grown, complex social orders. As Hayek states:

Even two hundred years after Adam Smith's *Wealth of Nations*, it is not yet fully understood that it is the great achievement of the market to have made possible a far-ranging division of labour, that it brings about a continuous adaption of economic effect to millions of particular facts or events which in their totality are not known and cannot be known to anybody.... A system of market-determined prices is essentially a system which is indispensable in order to make us adapt our activities to events and circumstances of which we cannot know.... [N]eoclassical economics, never clearly brought out what I call the "guide" or "signal function" of prices. That was due to the survival of the simple causal explanation of values and prices, assuming that values and prices were determined by what had been before rather than as a signal of what people ought to do (1983: 19; 35-36).

It is this understanding of the spontaneous emergence of a complex, and beneficial, social order that informed Adam Smith's arguments for economic liberty and against the restraints of trade. The voluntary action of thousands of individuals, each pursuing his own interests, generates and utilizes economic information that is not available to any one individual or group of individuals in its totality.³ Economic coordination relies upon the utilization of "local" or contextual knowledge (or what Hayek later terms knowledge of particular time and place) and not abstract "data." It is this emphasis on the use of contextual knowledge that underlies the critical defense of the liberal order from Smith to Hayek.

Consider, for example, Smith's discussion in his *The Theory of Moral Sentiments* concerning spontaneous order processes.

The man of system ... is apt to be very wise in his own conceit, and is often so enamored with the supposed beauty of his own ideal plan of government, that he cannot suffer the smallest deviation from any part of it. He goes on to establish it completely and in all its parts, without any regard either to the great interests or to the strong prejudices which may oppose it: he seems to imagine that he can arrange the different members of a great society with as much ease as the hand arranges the different pieces upon a chess-board; he does not consider that the pieces upon the chess-board have no other principle of motion besides that which the hand impresses upon them; but that, in the great chess-board of human society, every single piece has a principle of motion of its own, altogether different from that which the legislature might choose to impress upon it. If those two principles coincide and act in the same direction, the game of human society will go on easily and harmoniously, and is very likely to be happy and successful. If they are opposite or different, the game will go on miserably, and the society must be at all times in the highest degree of disorder (1759: 380-381).

Smith's case for economic liberty amounts to an argument and demonstration that individuals pursuing their self-interest can, and will, produce a social order that is economically beneficial.⁴ On the other hand, government restraint of trade not only cannot gain access to the knowledge necessary to do the job in a reasonably effective manner, but also grants too much power to the agent that interferes with the free economic process.⁵

"A real understanding of the process which brings this about was long blocked," Hayek has argued, "by post-Smithian classical economics which adopted a labour or cost theory of value" (1983: 19). In addition, with David Ricardo's reformulation of Smith, the emphasis came to be much more concentrated on the long-run, static equilibrium outcome of economic activity. This trend became all the more apparent after the marginalist revolution in the 1870s with the rise of Walrasian general equilibrium and Marshallian partial equilibrium. Among the founders of the marginalist revolution, however, Carl Menger was unique in his emphasis on the spontaneous ordering of economic activity.⁶ Menger, for example, devotes all of Book 3 of his *Investigations* (1883) to examining social institutions that emerge spontaneously. "We can observe," he wrote, "in numerous social institutions a strikingly apparent functionality with respect to the whole. But with closer consideration they still do not prove to be the result of an intention aimed at this purpose, *i.e.*, the result of an agreement of members of society or of positive legislation. They, too, present themselves to us rather as 'natural' products (in a certain sense), as the unintended results of historical development" (1883: 130). The examples of money, law, language, markets and communities are presented to demonstrate the prevalence of "organically" grown social institutions.⁷

For the proper study of these institutions, Menger emphasized, the social analyst cannot borrow the methods of the natural sciences. Rather, social theory requires the development of its own methods. Social institutions "simply cannot be viewed and interpreted as the product of purely mechanical force effects. They are, rather, the result of human efforts, the efforts of thinking, feeling, acting human beings" (1883: 133). Social institutions arise either due to a "common will directed toward their establishment" or as "the unintended result of human efforts aimed at essentially individual goals." In the second case, complex social phenomena "come about as the unintended result of individual human effort (pursuing individual interests) without a common will directed toward their establishment" (1883: 133).

While recognizing the importance of social institutions that emerge out of conscious design, Menger (1883: 146) did argue that it is in explaining institutions which arise spontaneously that social theory is dealing with the

most noteworthy problem of the social sciences. Moreover, Menger went on to argue that:

The solution of the most important problems of the theoretical sciences in general and of theoretical economics in particular is thus closely connected with the question of theoretically understanding the origin and change of 'organically' created social structures (1883: 147).

In order to demonstrate the power of spontaneous order explanations, Menger utilizes the example of the origin of money. A common medium of exchange emerges not as a product of anyone's design but as a result of individuals striving to better their condition.

Ludwig von Mises, who remarked that it was upon reading Menger's *Principles* that he became an economist (1978: 33), argues that Carl Menger's theory of the origin of money represents "the elucidation of fundamental principles of praxeology and its method of research" (1966: 405). Mises's vast contributions to economic science derive from his consistent application of what he called subjectivism to all areas of economic theory. This perspective is perhaps most vivid in his work on economic calculation and the importance of the institutions of private property and freely fluctuating money prices.

In his first major work, *The Theory of Money and Credit* (1912), Mises already pointed out the connection between private property, monetary calculation and the dynamic market process. "The phenomena of money," Mises argued, "presupposes an economic order in which production is based on division of labor and in which private property consists not only in goods of the first order (consumption goods), but also in goods of the higher order (production goods)" (1912: 41). And, this active process of exchange and production, in which money serves the indispensable function of facilitating coordination, is best understood as an interactive process of human evaluations and perceptions. As Mises wrote, it is a process which is "anchored deep in the human mind" (1912: 153).

The active process of bidding money prices up when demand exceeds supply and down when supply exceeds demand produces both the economic knowledge and incentives for various and diverse individuals to orient their actions toward each other. The system of monetary calculation "guides" individuals in their plan making. The problem with socialism, Mises contended, was that in the absence of this seemingly chaotic rivalrous process there was no way that economic planners could obtain the economic knowledge necessary to decide which of the various technologically feasible projects were economically feasible. Without private property in the means of production, there would be no markets for these goods. And, without a market for the means of

production, there could not be any money prices established to reflect the relative scarcities of these goods. In the absence of money prices reflecting the relative scarcities of higher order goods, there would be no way to know which projects are economically feasible and which ones were not (see Mises 1920 and 1922).

Economic calculation, despite its imperfections, provides knowledge to individuals so they may separate from among the multitude of technologically feasible projects those which are economic. Freely fluctuating prices, and the economic calculation it affords, work to solve the generalized knowledge problem that society confronts. It is the market process's ability to reveal error and motivate learning that underlies its claim of superiority in dealing with the problem of dispersed knowledge in society.⁸ Hayek's research throughout his career has elaborated on this Misesian insight, both in its positive form of the ability of the market process to convey the necessary economic knowledge for successful plan coordination and negative form of socialism's impossibility and interventionism's ineffectiveness at doing so.

III. Human Agency, Meaning and Social Theory

The human sciences begin with:

what men think and mean to do: from the fact that the individuals which compose society are guided in their actions by a classification of things or concepts which has a common structure and which we know because we, too, are men (Hayek 1952a: 57).

The data of the human sciences, in fact, "are what the acting people think they are" (1952a: 44). Indeed, as Hayek puts it, the human sciences, and economics, in particular, could be described:

as a metatheory, a theory about the theories people have developed to explain how most effectively to discover and use different means for diverse purposes (1988: 98).

We interpret the meaning individuals place on events because we "interpret the phenomena in light of our own thinking" (1952a: 135). These interpretations are not perfect and may not even be correct in any particular case, Hayek points out, but it is:

the only basis on which we ever understand what we call other people's intentions, or the meaning of their actions; and certainly the only basis of all our historical knowledge since this is all derived from the understanding of signs or documents (1952a: 135).

Not only do we rely upon our understanding of others, that we derive from our self-understanding, to theorize, but also in order to orient our actions to those of others. The pre-theoretical understanding of others, that is conveyed to us through language, enables us to cooperate socially with those who confront us anonymously. As Hayek states:

All people, whether primitive or civilised, organise what they perceive partly by means of attributes that language has taught them to attach to groups of sensory characteristics. Language enables us not only to label objects given to our senses as distinct entities, but also to classify an infinite variety of combinations of distinguishing marks according to what we expect from them and what we may do with them.... all usage of language is laden with interpretations or theories about our surroundings (1988: 106).

Our common-sense understanding of 'the other,' which comes to us through language, provides an invaluable source of knowledge in social understanding, both at the theoretical level and in our day-to-day existence. "It would be impossible," Hayek says, "to explain or understand human action without making use of this knowledge" (1952a: 43-44). Try to imagine, Hayek argues, what the social world would look like:

if we were really to dispense with our knowledge of what things mean to the acting man, and if we merely observed the actions of men as we observe an ant heap or a beehive. In the picture such a society study could produce there could not appear such things as means or tools, commodities or money, crimes or punishments, or words or sentences; it could contain only physical objects defined either in terms of the sense attributes they present to the observer or even in purely relational terms. And since the human behavior toward physical objects would show practically no regularities discernible to such an observer, since men would in a great many instances not appear to react alike to things which would to the observer seem to be the same, nor differently to what appeared to him to be different, he could not hope to achieve an explanation of their actions unless he had first succeeded in reconstructing in full detail the way in which men's senses and men's minds pictured the external world to them. The famous observer from Mars, in other words, before he could understand even as much of human affairs as the ordinary man does, would have to reconstruct from our behavior those immediate data of our mind which to us form the starting point of any interpretation of human action (1952a: 105).

Interpretation and understanding is only possible because we possess a pretheoretical understanding of what it means to be human. In other words, it is only because we can attribute *meaning* to human action that we can understand the diverse patterns of actions that make up the social world.

The key question for the social theorist is how the various and diverse images of reality that individual minds develop could ever be coordinated to one another. The social institutions that arise through the voluntary association of thousands of individuals serve to guide individuals in the process of mutual accommodation. The voluntary interaction of individuals reveals the various subjective pattern of trade-offs that individuals possess and utilizes this knowledge to promote plan coordination.⁹

Market participants, for example, do not possess knowledge of the real underlying economic factors in the economy. On the basis of *understanding*, individuals interpret the meaning of changes on the economic scene and orient their behavior accordingly. They rely on the freely established exchange ratio in the market to inform them about (1) current market conditions, (2) the appropriateness of past decisions, and (3) the future possibilities of pure profit. The market system provides *ex ante* information in the form of money prices reflecting the relative scarcities of goods so that economic actors may plan their future actions. The market system also provides *ex post* information through the system of profit and loss to inform market participants about the appropriateness of their past actions. If they bought cheap and sold dear they are rewarded, whereas if they bought dear and sold cheap they suffer losses. The array of market prices, however, also possess information about the possibility of pure entrepreneurial profit. The discrepancy between the current array of prices and the possible future array generates the discovery of ever new and fresh ways to shuffle or reshuffle resources in a manner that satisfies the demands of consumers. The market system as a whole, in its *ex ante*, *ex post* and discovery capacity, generates and utilizes economic knowledge "so tens of thousands of people whose identity could not be ascertained by months of investigation, are made to use the material or its products ... in the right direction" (Hayek 1945: 87).¹⁰

Social life, however, is not restricted to the market but encompasses a vast array of complex structures which enable us to successfully plan our actions in reference to others. The same procedure by which we understand successful plan coordination on the economic scene is applicable to other areas of our social existence. As Hayek has pointed out:

While at the world of nature we look from the outside, we look at the world of society from the inside; while, as far as nature is concerned, our concepts are about the facts and have to be adapted to the facts, in the world of society at least some of the most familiar concepts are the stuff from which the world is made. Just as the existence of a common structure of thought is the condition of the possibility of our communicating with one another, of your understanding what I say, so it is also the basis on which we all interpret such

complicated social structures as those which we find in economic life or law, in language, and in customs (1943: 76).

Though the complex structures of society are the composite of the purposive behavior of individuals, they are not the result of conscious human design. The intentional, *i.e.*, meaningful, behavior of individuals affirm or reaffirm the overall order in society. But social order is not the result of conscious design and control.¹¹ Perhaps the greatest source of misunderstanding in our social world is the failure to view society as an interpretive process which translates meaningful utterances of the human mind into socially useful knowledge, so that the various anonymous actors on the social scene may come into cooperation with one another, even though this order is not any part of their intention. As Hayek states:

We still refuse to recognize that the spontaneous interplay of the actions of individuals may produce something which is not the deliberate object of their actions but an organism in which every part performs a necessary function for the continuance of the whole, without any human mind having devised it. In the words of an eminent Austrian economist [Mises], we refuse to recognize that society is an organism and not an organisation and that, in a sense, we are part of a 'higher' organised system which, without our knowledge, and long before we tried to understand it, solved problems the existence of which we did not even recognise, but which we should have had to solve in much the same way if we had tried to run it deliberately (1933b: 130-131).¹²

Much of Hayek's work, including his work on the common law and his recent statements on the co-evolution of reason and tradition, follows directly from his exploration of Mises's discussion of the foundation of a social order based on the division of labor. The Hayekian research program extends the spontaneous order approach beyond the realm of economic explanation to all realms of social interaction, including science, law, and history. Hayek's economics has sought to articulate the discovery role of the competitive market process, his legal philosophy has sought to examine the discovery process of the common law, and his philosophical anthropology explores the discovery process of history.

IV. Hayek, Rationalism and the Law of Association

Law and principles of just conduct, rather than being the products of pure reason, evolve over time and take on new meaning as they are applied in new circumstances to resolve social conflicts. The recognition of the spontaneous ordering of social cooperation does not demean reason – in fact, it upholds man's reason in ordering his own affairs. Much of Hayek's work should be

seen as an attempt to defend reason against its abuse under the guise of *scientism* or Cartesian rationalism. Consider the following statements from Hayek's work on the liberal society:

Complete rationality of action in the Cartesian sense demands complete knowledge of all relevant facts. A designer or engineer needs all the data and full power to control or manipulate them if he is to organize the material objects to produce the intended result. But the success of action in society depends on more particular facts than anyone can possibly know. And our whole civilization in consequence rests, and must rest, on our believing much that we cannot know to be true in the Cartesian sense (1973: 12).

What we have attempted is a defense of reason against its abuse by those who do not understand the conditions of its effective functioning and continuous growth. It is an appeal to men to see that we must use our reason intelligently and that, in order to do so, we must preserve the indispensable matrix of the uncontrolled and non-rational which is the only environment wherein reason can grow and operate effectively (1960: 69).

What Hayek's work does deny is that the complex order of society is a result of rationalist construction and human design. The order that emerges under a system of division of labor and private property was not the result of anyone's design or intention, but was the composite of all the separate striving of individuals to realize their purposes and plans.

The social order made possible by the division of labor, Mises argued, was a result of the recognition of the benefits of such an order. The greater productive capabilities of the division of labor alert men to the gains of social cooperation. In this manner Mises generalizes Ricardo's principle of comparative advantage into the principle of association (see 1922: 256ff., 1966: 143ff.).

Much controversy surrounds Hayek's recent attempts to reformulate this principle and his use of cultural evolution in the explanation of the principle.¹³ For example, David Ramsey Steele (1987) has argued that Hayek has abandoned the social theory project of the Scottish Enlightenment and embraced a holistic approach to social analysis that is alien to both that tradition and Hayek's earlier work on methodological individualism. Hayek's theory of group selection and cultural evolution is at best incorrect, and quite possibly damaging to the classical liberal project.¹⁴ Hayek is reduced, Steele argues, by the logic of his own argument, to a naive conservative.

Viktor Vanberg (1986) raises a very similar criticism of Hayek's theory of cultural evolution. "A closer examination of Hayek's writings on this topic," Vanberg (1986: 83) argues:

reveals that, in actual fact, he neither systematically elaborates nor consistently pursues such an individualistic, evolutionary approach to the question of why it is that rules can be expected spontaneously to emerge that increase the efficiency of the group as a whole and that provide solutions to "problems of society."

There is, Vanberg concludes, a tacit shift in Hayek's work from his earlier methodological individualism, where behavioral regularities emerge from the rational assessment of trade-offs among social participants, to the quite different emphasis on social rules which are followed because of the benefits that accrue to the group. This shift, to Vanberg, is undesirable and unjustified, and undermines our attempt to grapple with the problem of rule formation in social processes.

James Buchanan (1977, 1986a) has also reiterated these criticisms. But Buchanan's criticism is more fundamental. He challenges the very idea of extending the spontaneous order paradigm beyond the realm of economics. While the discovery process of competitive markets tends to produce some optimality conditions (sub-optimality is eliminated in the pursuit of pure profit), there is no guarantee that legal processes yield the same result and certainly the discovery process of history cannot be relied upon. Buchanan finds Hayek's arguments about diffuse knowledge and the discovery process of the market convincing, but the extension of the argument to other social institutions creates problems, he believes, for grappling with what he calls the constitutional level of political economy. Hayek's conservatism doesn't allow for the deliberate reform of the rules of society. "There is no room left," Buchanan argues, "for the political economist, or for anyone else who seeks to reform social structures, to change laws and rules, with an aim of securing increased efficiency in the large" (1986a: 76).

Even Israel Kirzner, perhaps the leading representative of the modern Austrian school, follows Buchanan's essentially equilibrium criticism of Hayek. Kirzner is concerned that Hayek's extension of the spontaneous order approach beyond economics may lead us astray and undermine the defense of economic liberty. "The extraordinary power of arguments rooted in market theory should not be compromised," Kirzner warns, "by well-meaning but unhelpful reference to other kinds of spontaneous order" (1987: 46).

Kirzner distinguishes between traditional spontaneous order explanations found in the writings of Adam Smith, *etc.*, which assumed individuals acting with regard to their self-interest within a given institutional framework, and the more recent literature on spontaneous order which emphasizes the plausibility of social coordination emerging out of the self-interested behavior of individuals within an environment without any given institutional framework. While

the earlier work was able to demonstrate, Kirzner argues, that within a certain institutional environment the decentralized decisions of economic actors could be coordinated in a manner which allocated resources in an "objectively" efficient manner, the later work does not possess such a logic – there are no equilibrium conditions in law, language and custom.

Both Buchanan and Kirzner explicitly rely on the neoclassical description of competitive markets as Pareto Optimal. Buchanan, for example, argues that there are three reasons to adopt spontaneous order explanations: political, aesthetic, and economic. Political, because of a proper understanding of the spontaneous ordering of economic activity in a competitive market will possess tremendous import for economic policy decisions. Aesthetic, because spontaneous order explanations are intellectually more satisfying than expectations from design. Economic, because an understanding of spontaneous order allows us to "say that the workings of the market generate Pareto-efficient results" (1977: 29). But this third reason for adopting spontaneous order explanations of social coordination also limits their normative application beyond technical economics. We simply cannot say that either the legal or historical process possesses any logic which generates Pareto-efficient results. While the competitive market harbors tendencies to equilibrate and thus eliminate socially undesirable states of affairs, "the forces of social evolution ... contain within their workings no guarantee that socially efficient results will emerge over time." The social institutions which emerge "need not be those which are the 'best'" (1977: 31). Or, as Kirzner has put it:

There is no guarantee that the English language my children learn at their mother's knee will be a 'better' language for purposes of social intercourse than, say, French – or Esperanto. The demonstration that widely accepted social conventions can emerge without central authoritarian imposition does not necessarily point to any optimality in the resulting conventions.

What is demonstrated in the spontaneous order explanation of free market process, on the other hand, "is that there does exist a spontaneous tendency toward social optimality under the relevant conditions" (1987: 48).

The Achilles heel of these criticisms, however, is their continued reliance on the neoclassical notion of optimality. The Hayekian program has become increasingly disillusioned with any idea of optimality conditions and equilibrium states as these concepts proved to frustrate rather than enhance our understanding of social interaction, as Buchanan himself has recognized (1986b: 73-74). As Hayek has put it:

I am afraid that I have become – with all aesthetic admiration for the achievement – more and more sceptical of the instructive value of the construction by which at one time I was greatly fascinated, that beautiful system

of equations with which we can show in imagination what would happen if all these data were given to us. But we often forget that these data are purely fictitious, are not available to any single mind, and, therefore, do not really lead to an explanation of the process we observe (1983: 36).

The modern Austrian school, following Hayek, has sought to consistently advance an alternative approach to the study of economic activity. The Austrian theory of the market process stands in stark contrast to the more traditional equilibrium analysis of mainstream neo-classical economics. A theoretical perspective has developed which is built around both a deep appreciation of the subjective nature of the economic world and a recognition of how social institutions work through the filter of the human mind to coordinate activity. This economic process is neither an evolutionary natural selection process that assures the survival of the "best" or "fittest" nor is this process a chaotic and random walk. The discovery process of the competitive market is a learning process – a process of trial and error and experimentation in which the key component is the ability to reveal error and motivate the discovery of new knowledge about economic opportunities.

As Kirzner and Buchanan have themselves demonstrated, the market process does not lead to any optimal state. The market process is misspecified if presented as an equilibrium system. Free market processes are characterized by continuous sub-optimality – in fact, that is what generates the whole process of learning and discovery. The superiority of the market process, as pointed out above in the discussion of economic calculation, lies not in its ability to produce optimal results, but rather in its ability to mobilize and effectively use knowledge that is dispersed throughout the economic system.

The criticism of Hayek's project on the grounds of his abandonment of methodological individualism, moreover, are misplaced for two reasons.¹⁵ First, Hayek is mainly talking about the co-evolution of reason and tradition in the epoch when man was first emerging from his pre-human condition. Hayek's thesis is that our reason developed because we followed certain rules, not that we followed certain rules because of our reason. As he writes, cultural evolution:

took place not merely after the appearance of *Homo sapiens*, but also during the much longer earlier existence of the genus *Homo* and its hominid ancestors. To repeat: mind and culture developed concurrently and not successively (1979: 156).

This leads to a position which challenges the sort of isolated and atomistic methodological individualism characteristic of much economics. Social inquiry must begin with a recognition of the social embeddedness of the mind. As Chris Sciabarra argues:

For Hayek, the individual cannot stand by himself – he is invariably an actor in a specific historical and cultural context. Hayek's arguments have an epistemological dimension as well. For Hayek, there is a limit beyond which we are unable to articulate the rules, customs and habits which govern our lives. We are internal to these rules and cannot take an external, transcendental role. To this end, even our consciousness operates according to rules of which we are not conscious – since these rules are internal to the operation itself (1987: 90-91).

Second, the best way to understand what Hayek is trying to do in *The Constitution of Liberty*, *Law, Legislation and Liberty* and *The Fatal Conceit* is to restate and elaborate from a consistently non-rationalist perspective, the Mises's argument concerning the Law of Association. "We have never designed our economic system," Hayek states. "We were not intelligent enough for that" (1979: 164). Hayek is offering, as John Gray (1986: 130) points out:

a more humble, sceptical and modest form of liberalism than that found in the French philosophers, a liberalism that has rid itself of the incubus of an hubristic rationalism – and which has most in common with the social philosophy of the thinkers of the Scottish Enlightenment, and, above all, with the outlook of David Hume. Hayek is, in effect, refining and completing this non-rationalist tradition of classical liberalism.¹⁶

As Hayek writes in *The Fatal Conceit*:

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 of population and wealth – of those groups that happened to follow them (1988: 6).

The institution of private (or separated) property, which man stumbled into, according to Hayek, made possible the growth of civilization. By following certain rules, which he could not justify nor even state, man cultivated his social world.¹⁷ "Such activities in which we are guided by a knowledge merely of the principle of a thing," Hayek states, "should perhaps better be described by the term *cultivation* than by the familiar term 'control'" (1955: 19, emphasis in original).

Hayek argues that the coincidence of opinion concerning just rules of conduct will emerge through the purposive and meaningful dialogue of human interaction. Implicit rules of conduct will be respected among the various individuals in the social world before agreement is reached on articulated rules.

It is these implicit rules through which the law of association operates to bring about the liberal extended order.

"It is only as a result of individuals observing certain common rules," Hayek argues, "that a group of men can live together in those orderly relations which we call society" (1973: 95). Man does not need to consciously recognize the benefits of society as a whole, but merely the benefits to him of the division of labor and exchange. Out of a process by which individuals strive to improve their lot in life, the rules of the extended order come to be respected. Neither do we need to live in a world where every other man believes as we do about fundamental values in order to live in harmony. All we need are rules or social institutions (conventions, symbols, *etc.*) that produce mutually reinforcing sets of expectations to maintain a degree of social order, and these rules or institutions must serve as guides to individuals so they may orient their actions. The rules of social intercourse must be rigid enough so as to confirm our expectations, but flexible enough to allow for changing circumstances and creative human potential. As Hayek argues:

Living as members of society and dependent for the satisfaction of most of our needs on various forms of cooperation with others, we depend for the effective pursuit of our aims clearly on the correspondence of the expectations concerning the actions of others on which our plans are based with what they really do (1973: 36).

Civilization can be cultivated through the judicious use of reason, but its complexity lies beyond the ability of human reason to design or control it. As Hayek states in *The Counter-Revolution of Science*:

We flatter ourselves undeservedly if we represent human civilization as entirely the product of conscious reason or as the product of human design, or when we assume that it is necessarily in our power deliberately to re-create or to maintain what we have built without knowing what we were doing. Though our civilization is the result of a cumulation of individual knowledge, it is not by the explicit or conscious combination of all this knowledge in any individual brain, but by its embodiment in symbols which we use without understanding them, in habits and institutions, tools and concepts, that man in society is constantly able to profit from a body of knowledge neither he nor any other man completely possesses. Many of the greatest things man has achieved are the result not of consciously directed thought, and still less the product of deliberately coordinated effort of many individuals, but of a process in which the individual plays a part which he can never fully understand. They are greater than any individual precisely because they result from the combination of knowledge more extensive than a single mind can master (1952a: 149-150).

V. Conclusion

Hayek's social theory is carrying on and advancing the tradition of social analysis that dates back to the Scottish Enlightenment thinkers, such as David Hume and Adam Smith. His work, and especially his scholarly example, serves as an inspiration to several younger scholars who are attempting to stand on his shoulders and push his insights on the social world even further.

Hayek has claimed, for example, that the coercive powers of the State have corrupted the social institutions of money and law. He has himself suggested a framework to study these problems, but it is in the work of several younger scholars that these problems are now being explored in detail.¹⁸ For some time his followers will be, as Hayek said of Mises, "pursuing the questions which he made [them] see" and that is the greatest gift one scientist can give to another.

NOTES

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¹ Gray has most recently come to interpret Hayek as a naive conservative who abandons methodological individualism in his later work on social anthropology. This, however, is a misreading of Hayek as well be argued later in the paper. In fact, to a large extent, Gray's most recent repudiation of much of the liberal tradition of social philosophy results, ironically, from a serious misreading on his part. See Gray (1988) for a discussion of the problems he sees in the liberal project.

² See Hayek (1959a: 52, fn. 7) for a discussion of the importance of Mises's work for the advancement of economic understanding.

³ As Smith wrote in connection with the multitude of activities that must coordinated to produce a simple woollen coat: "Observe the accommodation of the most common artificer or day-labourer in a civilized and thriving country, and you will perceive that the number people of whose industry a part, through but a small part, has been employed in procuring him this accommodation, exceeds all computation" (1776: 15).

⁴ This, of course, requires certain well-specified rules under which individuals are pursuing their individual interests, for example, the right of property. In the absence of private property, Smith would not be surprised by the "tragedy of the commons" problem.

⁵ See Smith (1776: 478). This of course, conflates the two arguments – the use of knowledge and the abuse of power – and it is not until after Mises's and Hayek's work concerning the problem of socialist calculation that the focus shifts to concentrate more directly on the use of knowledge in society. Nevertheless the argument is presented in embryonic form in Smith, as Hayek (1988: 14, 86-87) points out.

⁶ See William Jaffe (1976: 518-519; 520) where he argues that:

Carl Menger clearly stands apart from the other two reputed founders of the modern marginal utility theory. ... It is not that Menger was unaware of tendencies to eventual equilibrium in the real world, but he was too conscious of the ubiquitous obstacles that, even *ceteris paribus*, impede the attainment of market equilibrium within anything less than secular delays. With his attention unswervingly fixed on reality, Menger could not, and did not, abstract from the difficulties traders face in any attempt to obtain all the information required for anything like a pinpoint equilibrium determination of market prices to emerge, nor did his approach permit him to abstract from the uncertainties that veil the future, even the near future in the conscious anticipation of which most present transactions take place.

⁷ As Menger stated, though, "The organic view cannot be a universal means of consideration; the organic understanding of social phenomena cannot be the universal goal of theoretical research in the field of the latter. Rather, for the understanding of social phenomena in their entirety the pragmatic interpretation is, in any case just as indispensable as the 'organic'" (1883: 135). For a recent discussion of this line of argument see Witt (1989).

⁸ Much of Mises's work, and especially the work of his student Israel Kirzner, on the nature of the market system and the entrepreneurial process, is an attempt to demonstrate how the institutions of a free market overcome the generalized knowledge problem that faces society. That is, how do social institutions serve to coordinate the dispersed, and often conflicting, plans of various actors in society? As Kirzner (1984: 415) argues, "The truth is that the market does possess weapons to combat (if not wholly to conquer) the problem of dispersed knowledge. These weapons are embodied in the workings of the price system, but not in the workings of a hypothetical system of equilibrium prices. The importance of prices for coping with the Hayekian knowledge problem does not lie in the accuracy of the information which equilibrium prices convey concerning the actions of others who are similarly informed. Rather, its importance lies in the ability of disequilibrium prices to offer pure profit opportunities that can attract the notice of alert, profit-seeking entrepreneurs. Where market participants have failed to coordinate their activities because of dispersed knowledge, this expresses itself in an array of prices that suggests to alert entrepreneurs where they may win pure profits."

⁹ As Thomas Sowell writes about the decentralized process of market exchange and production: "Prices convey the experience and subjective feelings of some as effective knowledge to others; it is implicit knowledge in the form of an explicit inducement. Price fluctuations convey knowledge of changing trade-offs among changing options as people weigh costs and benefits differently over time, with changes in tastes and technology. The totality of knowledge conveyed by the innumerable prices and their widely varying rates of change vastly exceeds what any individual can know or needs to know for his own purposes" (1980: 167).

¹⁰ The development of this process cultivates the operation of advanced technological developments that depend upon the system's ability to mobilize the dispersed knowledge of thousands of individuals. As Lavoie argues: "the evolution of markets has delivered us into a world too complex for any individual intelligence to comprehend in detail, thus necessitating our reliance on the greater social intelligence embodied in market processes. These market processes, if they are to generate and embody a high degree of social intelligence, require relatively free competition among (*de facto*) private owners of capital

and other resources and the continuous (and nonegalitarian) ebb and flow of wealth caused by this competitive process" (1985b: 51).

¹¹ See Hayek (1976: 107-132) for a discussion on how the economizing behavior of individuals gives rise to the catallactic order even though that was no part of their intention.

¹² Hayek's reference on this point is quite important and challenges those who wish to differentiate Mises from Hayek on their view of spontaneous processes of mutual accommodation. As Mises wrote in the section Hayek alludes to in the quote, "Organization is an association based on authority, organism is mutuality In recognizing the nature of the organism and sweeping away the exclusiveness of the concept of organization, science made one of its great steps forward. With all deference to earlier thinkers one may say that in the domain of Social Science this was achieved mainly in the eighteenth century, and that Classical Political Economy and its immediate precursors played the chief part" (1922: 262-263).

¹³ See, for example, the criticism of Hayek's project in Gray (1986: 116ff.) and (1988), Buchanan (1977, 1986a), Vanberg (1986), Steele (1987) and Miller (1989).

¹⁴ While Steele bemoans this, Geoffrey Hodgson (1988, 1989) rejoices in the inconsistency of Hayek's liberal project. Hayek's abandonment of "abstract individualism," Hodgson argues, undermines the case for the liberal society even if Hayek fails to recognize it. The breakdown of the classical liberal bias in economic science is a major advance, Hodgson argues. I will suggest, however, that (1) we should not be concerned with whether Hayek's project defends or undermines a certain set of policies, but rather that it aids us in understanding the world and that, as it turns out, (2) Hayek's argument actually does enhance his argument for classical liberalism.

¹⁵ See Yeager (1989) for a defense of Hayek against those who misread him as undermining human reason. As Yeager argues, Hayek "recognizes that in the evolution of the Common Law, for example, judges decided individual cases by trying rationally to identify, articulate and apply practices and rules already in effect, though not yet explicitly recognized. And he certainly accepts Carl Menger's account of the spontaneous evolution of money, according to which individuals rationally adopted practices that facilitated their transactions" (1989: 327).

¹⁶ Also see Herzog (1986) for a discussion of the importance of the Hume-Smith project for social theory.

¹⁷ Those who argue that Hayek's emphasis on the population growth that is made possible through private property is a deviation from the classical liberal tradition should remember that Adam Smith argued that "The most decisive mark of the prosperity of any country is the increase of the number of its inhabitants" (1776: 79). And, moreover, Mises argued that the choice between capitalism and socialism was a choice between property and freedom versus starvation, death and barbarism. As Mises wrote: "Whether Society is good or bad may be a matter of individual judgment; but whoever prefers life to death, happiness to suffering, well-being to misery, must accept society. And whoever desires that society should exist and develop must also accept, without limitation or reserve, private ownership in the means of production" (1922: 469).

¹⁸ On money see White (1984) and Selgin (1988) and on law see Barnett (1985 and 1986) and Benson (1988) for some of the attempts to grapple with these problems.

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