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Review essay: The young Hayek  
by Ivo Maes



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## Abstract

Friedrich Hayek has been one of the dominating intellectual figures of the 20th century. Hayek, together with Gunnar Myrdal, received the 1974 Nobel Memorial Prize in economics, for “their pioneering work in the theory of money and economic fluctuations and for their penetrating analysis of the interdependence of economic, social and institutional phenomena”. Bruce Caldwell (Duke University) and Hansjoerg Klausinger (WU Vienna University of Economics and Business), two distinguished historians of economic thought, have produced a massive (840 pages) work, covering the first five decades of Hayek’s existence. *Hayek: A Life, 1899-1950* is a monumental and sympathetic biography. The book is based on painstaking archival research and shows great scholarship. The novelty is very much in bringing the person of Hayek to life, with its strengths and weaknesses.

Keywords: Friedrich Hayek, Austrian school, biography, business cycle theory.

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Friedrich Hayek has been one of the dominating intellectual figures of the 20<sup>th</sup> century. Hayek, together with Gunnar Myrdal, received the 1974 Nobel Memorial Prize in economics, for “their pioneering work in the theory of money and economic fluctuations and for their penetrating analysis of the interdependence of economic, social and institutional phenomena”. Bruce Caldwell (Duke University) and Hansjoerg Klausinger (WU Vienna University of Economics and Business), two distinguished historians of economic thought, have produced a monumental (840 pages) biography of the first five decades of Hayek’s life, *Hayek: A Life, 1899-1950*. It is a thoroughly researched and scholarly work. Unfortunately, in a relatively short review essay as this, it will not be possible to do full justice to all aspects of this volume.

In the Introduction, Caldwell and Klausinger describe the origins of the project. In the last decade of his life, Hayek accepted an invitation to participate in two interrelated projects, a full biography and a book series that would collect his writings. The American philosopher W.W. (Bill) Bartley III was to serve as both Hayek’s biographer and the General Editor of the “*Collected Writings of F.A. Hayek*”. Unfortunately, he passed away in 1990. The biography languished, but the “Collected Works” continued under the editorship of Stephen Kresge. In 2002, Kresge asked Bruce Caldwell to take over as the third General Editor. Caldwell was further keen to take up the role of Hayek’s biographer. A problem was that Hayek had always insisted his biographer be fluent in German (which was not the case for Caldwell). Caldwell invited then Hansjoerg Klausinger to join him. The Hayek family provided access to all the existing family correspondence and other materials. Caldwell and Klausinger could then draw on a wealth of new archival material. As they admit themselves, their aim is ambitious, “the definitive full biography of F. A. Hayek” (p. 3). They are working on a second volume, covering the second part of Hayek’s life.

The book is divided in six, chronological, parts: “A Viennese youth”, “A broadening of horizons”, “The making of an economist”, “Hayek in 1930s England”, “Fighting the spirit of the age” and “Changing worlds”. The first part, “A Viennese youth”, explores the period from Hayek’s birth in 1899 to his military service in World War One. It offers a captivating picture of fin-de siècle -Vienna, the capital of the Austro-Hungarian empire, a place of strong creative tensions. There was a thriving and generally well integrated Jewish community (many famous economists of the Austrian school were Jewish)<sup>1</sup>. But Vienna was also a place of destructive political, religious, and ethnic divisions. As the monarchy gradually lost its grip on society, an age of increasingly raw and nasty mass politics began, with many varieties of fanaticism on offer: Marxist, fascist, anti-semitic, pan-German, nationalist... Hayek’s family was upper middle class: conservative, Christian, and culturally German. In the summer, like most middle -class families, the Hayeks would go to the countryside. The young Hayek loved the mountains (it would remain a lifelong passion). He quickly developed an “independent streak” (p. 20) and would gradually move away from the influence of his family and milieu.

The second part, “A broadening of horizons”, focuses on the period 1918 to 1923. The Vienna to which Hayek returned after the war was a “shipwreck” (p. 87). He enrolled at the university, making also Jewish friends. Though nominally a law student, Hayek pursued his own interests, like philosophy, psychology and economics (with Friedrich Wieser as one of his professors).

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<sup>1</sup> As observed by Caldwell and Klausinger, “the vast majority of the Mises circle was of Jewish descent” (p. 203). Some of the (Jewish) participants were part of the (lower) nobility, like Ludwig von Mises himself, showing that Jewish people were quite well integrated in the Viennese society.

Together with Herbert Fürth (a very close Jewish friend from the Gymnasium), he founded a circle of his own, a discussion group that came to be called the “Geistkreis” (Mind Circle). During these years, he definitively turned away from the German nationalist perspective of his family toward the “liberal-progressive and cosmopolitan views held by those in the mixed groups of which he had become a member” (p. 154). He got a first job at the Austrian Clearing Office for War Debts, directed by Ludwig von Mises. In 1923 and 1924, he spent fifteen months in the United States. He studied in New York, where he got to know Wesley Clair Mitchell, the doyen of the American institutionalists and the founder of the National Bureau of Economic Research. He also acquired there an understanding of the statistics associated with industrial fluctuations and of the workings of the Federal Reserve. His American experience turned him into a young academic and exposed him to a wholly different culture (which he did not really like).

With part three, “The making of an economist”, the focus is on Hayek’s early career as an economist in Vienna. Mises invited him to his private seminar where he worked with economists like Gottfried Haberler, Fritz Machlup, and Oskar Morgenstern. Mises was also the driving force behind the creation of the Institute for Business Cycle Research, of which Hayek would become the first director. It would help Hayek to expand his professional networks, also internationally. During these years, Hayek actively pursued his “lifetime ambition” of becoming a professor (p. 196). He began to develop a series of theories about the functioning of a monetary economy. Hayek started from an intertemporal general equilibrium model. He introduced then monetary disturbances, which led to distortions in the structure of production, causing the trade cycle. In 1926, he married Hella Fritsch, who gave birth to a daughter in 1929. As observed by Caldwell and Klausinger, “By the turn of the decade, along with a daughter, the Hayekian theory of the cycle had been born” (p. 196).

In part four, “Hayek in 1930s England”, the focus is on Hayek’s early period at the London School of Economics (LSE). A key figure at the LSE was Lionel Robbins, who wanted to internationalize economics at the LSE. Robbins invited Hayek for a series of lectures, “*Prices and Production*”, in January 1931. They were a big success and contributed to an invitation for a visiting professorship, and, thereafter, a chair<sup>2</sup>. During the 1930s, Hayek fought some of his most important intellectual battles. The first of these was with John Maynard Keynes, with at the core their respective theories of a monetary economy. The second was the so-called “socialist calculation debate”. However, as observed by Caldwell and Klausinger, “Hayek had little success on the intellectual battlefield” (p. 272). This all happened in a time of unprecedented political and economic turmoil, with the Great Depression, the rise of fascism and the looming of a new war. In 1938, Hayek naturalized as a British citizen, as observed by Caldwell and Klausinger, “it also formally defined his relationship with Austria and the Nazi regime” (p. 431). The same year, his brother Heinz joined the Nazi party.

At the end of the 1930s, liberalism, the philosophy Hayek had come to embrace, was in eclipse. On the contrary, the idea of planning, to rationalize production and distribution decisions, was on the rise, with scientists and engineers playing “an integral role” (p. 435). This vision of a scientifically planned future was for Hayek the spirit of the age. As the title of

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<sup>2</sup> Hayek very much stuck to the arguments of “*Prices and Production*”, also in a lecture at the LSE for the 50<sup>th</sup> anniversary of the event (p. 380). This is also very much my personal memory, attending Hayek’s 1981 lecture as a student at the LSE.

part five, “Fighting the spirit of the age” tells us, Hayek disagreed fundamentally. Hayek embarked on a big book project “The Abuse and Decline of Reason”. The aim was to trace the origins of these ideas, from the French Revolution, and to show how they gradually spread to different countries. In the 1930s, progressive intellectuals very much agreed that planning was the best hope for constructing a world in which freedom and prosperity could exist. Hayek disagreed completely and wanted to show the “horrible consequences that these ideas had in the twentieth century” (p. 436). While he did not finish this great book project, it would lead to several essays as well as his most famous book, “*The Road to Serfdom*”. Part of the work on this project was done in Cambridge, where the LSE had moved to during the war. In this period, in 1937, Hayek also published an essay, “Economics and Knowledge”, in which he argued that one should regard competition not as a state of affairs, but as a process by which knowledge is dispersed and acquired. Later he even referred to this paper as his “only *original* contribution to economics” (as quoted on p. 511, original italics).

In the sixth chapter, “Changing worlds”, Caldwell and Klausinger discuss the period from the end of the war to 1950, when Hayek moved to the University of Chicago. It was a period of intense intellectual activity. Caldwell and Klausinger characterize “The Use of Knowledge in Society”, as “Hayek’s most famous economics paper” (p. 601). In this essay Hayek develops the argument that the price system enables economic agents to use the dispersed, localized knowledge that exists in the brain of other agents in the system. The book further discusses in detail Hayek’s role in the formation of the Mont Pèlerin Society, of which Hayek would become the first president. Moreover, as everywhere in the book, Caldwell and Klausinger discuss in detail Hayek’s private life. At the core is here Hayek’s wish to start a new life with an old Austrian friend, Lenerl, and to divorce from his wife Hella, with whom he had two children. The process of the divorce is discussed in more than considerable detail and is not always pleasant reading. As observed by Caldwell and Klausinger, “No one (with the possible exception of Lionel Robbins) came out of it looking very good, and everyone at various points looked quite bad” (p. 589). It was also the reason why Hayek lost, with an embittered Lionel Robbins, someone which he considered as one of his true friends. In the end, Hayek moved from the old to the new world, and this with a new wife and a new job.

Any biography involves painful decisions and choices. Caldwell and Klausinger have a, very honest, section in the Introduction on “Some decisions we made in writing this biography”. They, very rightly, state that a biography deals with a subject’s life, not just his ideas. They tell that they decided “to hold very little back” (p. 9). This concerns particularly that both of Hayek’s parents participated in Vienna’s anti-semitism as well as Hayek’s divorce. They also tell about their two-day manuscript conference, which helped them reshape (and shorten) the manuscript<sup>3</sup>. They further decided not to engage with the “existing critical literature” regarding Hayek, “we did not attempt to provide a critical assessment of his thought” (p. 8). They argue that, as historians of economic thought, “we sought to reveal what he did and said, and to explain what motivated him” (p. 8). I broadly agree that it is indeed crucial to explain the evolution of a person’s thought and place it in its context. However, one might argue that also the critical debates of the times can be important. In this regard, I’m a bit uneasy with their treatment of Sir John Hicks (who received the Nobel Memorial Prize in economics in 1972),

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<sup>3</sup> Personally, I have the impression that there was some further scope for shortening. For instance, four pages on “The decline and fall of William Beveridge” as a director of the LSE is quite long. Also, family stories are sometimes told in (painstaking) detail.

as well as the Hayek Hicks relationship at the LSE. Caldwell and Klausinger discuss different elements of the interaction between Hicks and Hayek, but not how Hicks became a “Keynesian”, starting from a request of Robbins to translate Hayek’s *“Prices and Production”* into mathematics (Hicks 1982: 6). Hicks started from the same type of intertemporal model as Hayek, with perfect foresight as a condition for equilibrium. Hayek then introduces monetary disturbances. But Hicks went into the question of the nature of money in this construction, “if the future course of economic data (and the corresponding future course of prices) were exactly foreseen, there would be no demand to hold money as money” (Hicks 1933: 527). Like for Keynes, the holding of money becomes for Hicks intimately connected with uncertainty and the disappointment of expectations (Maes 1990: 128). Hicks then abandoned the Hayekian idea to elaborate monetary theory in line with capital theory but introduced marginal analysis (of which he was one of the pioneers in the 1930s), foreshadowing modern portfolio theory, as developed later by James Tobin<sup>4</sup>.

*“Hayek: A Life, 1899-1950”* is a monumental and sympathetic biography of Friedrich Hayek. It is very well written, very clear and well structured. The book is based on painstaking archival research and shows great scholarship. The novelty is very much in bringing the person of Hayek to life, with its strengths and weaknesses.

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<sup>4</sup> Sir Paul Chambers, in his master’s thesis, advised by Robbins and Hayek, questioned Hicks’s view that “monetary theory falls outside equilibrium theory” (Chambers 1934: 3). In his view, not only risk, but also transaction costs determine the demand for money, an idea which, later, would also be taken up by Hicks and Tobin (see Maes 1991).



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