The Washington Times

# BOOK REVIEW: ‘The Clash of Economic Ideas’

THE CLASH OF ECONOMIC IDEAS: THE GREAT POLICY DEBATES AND EXPERIMENTS OF THE LAST HUNDRED YEARS
By Lawrence H. White
Cambridge University Press, $125, 430 pages

The clash of economic ideas perhaps has never been this bitter. The possible breakup of the eurozone may bring Europe into uncharted waters, but the debate over the future of the Continent is shaped by ideas that are at least a century old: restraint in public finance versus economic stimulus. John Maynard Keynes giggled: "Practical men, who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist."

Economics is a pluralistic science, but there is a single key question that still underpins the debates on economic policy: What role, if any, should the government play in the economy? Divergent answers to this question informed the great political experiments of the last century, from Russian collectivization to Thatcherite privatization in Britain.

In "The Clash of Economic Ideas: The Great Policy Debates and Experiments of the Last Hundred Years," George Mason economist Lawrence H. White provides a masterful treatment of the struggle between different approaches and different schools of thought. Mr. White's book is an uneasy cocktail: He beautifully mixes history of economic thinking, political history and bites of biography (each chapter begins with a vignette) that humanize economists for his readers but also convey a sense of the real excitement that research and policy advocacy can engender.

For Mr. White, the clash of economic ideas in the 20th century is best epitomized by the intellectual struggle between two men: John Maynard Keynes and Friedrich von Hayek. Mr. White's book is respectful and fair to Keynes, but the author - a leading contemporary proponent of the Austrian school - is firmly set in Hayek's camp.

The champions of Cambridge and Vienna are aptly portrayed in the first chapter of the book: Personal friends, they both somehow were reluctant converts to economics. It was the great Alfred Marshall that "pestered" Keynes, then "a clever graduate mathematics student," to turn professional economist, whereas Hayek read his first economic books in the trenches of World War I but was really turned on to the subjectby Carl Menger's "Principles of Economics."

"Keynes as a young man, and Hayek as boy, lived through a remarkable period of economic growth that accompanied the relatively market-friendly policies in the decades before 1914," Mr. White notes.

However, their responses to the collapse of the European equilibrium with the two world wars and to the Great Depression were polar opposites.

Keynes basically concluded that "the market economy had collapsed on its own, had become trapped in a vicious circle, and could not free itself." It needed, therefore, government help. The overall lack of demand leads to voluntary unemployment, and thus to reduce unemployment quickly, you need specific government policies.

Mr. White points out that Keynes' ideas were not completely novel when his "The General Theory of Employment, Interest and Money" was published: "Many leading and non-radical economists had proposed government spending on public works programs to relieve the unemployment of the early Great Depression." However, if those proposals already were around, Keynes' book appeared with pitch-perfect timing: The political classes wanted a rationale for the policies they already were implementing, and they thought it would begood to consolidate their voting bases.

Hayek came from a different background. Whereas Keynes focused mostly on labor markets, Hayek's approach was "capital-based macroeconomics." He reflected on the changing structure of capitalist production during the business cycle. This is why, at the time the Depression hit, Hayek's policy recommendation "to let output and employment on their own as bankruptcies and layoffs released workers and machines to find more suitable employments, was regarded by many as a counsel of despair."

To simplify: Keynes told political leaders they could do good here and now; Hayek emphasized unintended consequences. Hayek's background lay in the so-called "socialist calculation debate." The debate is thoroughly described in a crystal-clear chapter of Mr. White's book. It began in 1920, when Austrian economist Ludwig von Mises spotted the basic flaw of socialism: "Having abolished markets and thereby prices for the means of production, the directors of a socialist economy would not know how to combine resources to produce goods economically." In a free economy, "the market pricing process, driven by bidding from profit-seeking entrepreneurs, assigns prices to inputs according to their anticipated value added in producing consumer goods."

Prices work as a traffic light to production. They orient choices in a realm of scarcity, allowing for resources to find their better use. A market economy is not a static picture. It continuously evolves and adapts, as day after day interactions between economic players allow them to develop better and newer knowledge about how resources could be used. Mr. White quotes Mises: Decentralization in a world of scarcity "entails a kind of intellectual division of labor." Hayek departed from this to emphasize that the market system actually is a process in which continuous, mutual adaptation generates useful information.

In a way, it is more than a government-versus-markets debate - it is top-down versus bottom-up.

Hayek andhis followers, like Mr. White, have a fundamental difference with Keynes and his ilk - and it is an epistemological, not a technical, one. They would point out that we cannot trust a single decision-maker - be it a Soviet planner or a Western bourgeois minister - to know better than millions of people who make market transactions.

Planners' mistakes tend to be more expensive than individuals' because the consequences of their failures are wider in scope. Planners also are less resilient. Rather than alter their plans when proved wrong, they tend to twist facts to conform to their notions. Today's European Union provides a good illustration of this phenomenon.

The struggle of economic ideas is ultimately a philosophical battle between those who think individuals are better judges of what's best for them and those who think the government is.

Preachers of Keynesian government intervention typically have found a friendlier ear among the political class. But the game is still pretty open, and perhaps the staggering failure of governments and rulers in today's world may strike a blow for humility - and for Hayek.

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