

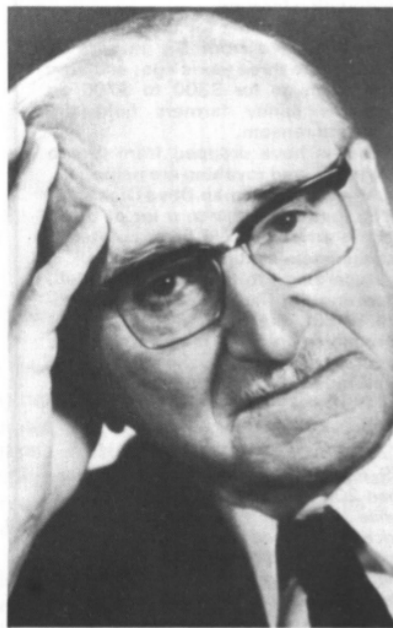
HAYEK, POVERTY, MORALITY AND THE FREE MARKET

KEYNES was wrong. According to Prof. Hayek, it is not aggregate demand but its distribution that determines the level of employment, and Keynes was mistaken in inferring from the special circumstances of Britain's return to the gold standard in 1925 that an increase in demand always stimulates employment. What is important is that the supply of particular goods and services is responsive to the demand for them: if the demanders seek more of one product and the suppliers produce more of another, the equation of total supply with total demand will not prevent a surplus of the 'wrong' product and the redundancy of those who manufacture it.

It is futile, then, to increase aggregate demand when what is required is the flexibility of suppliers to meet specific demands. Such flexibility is most easily attained when there is freedom for prices, including the price of labour, to move up or down and so indicate where resources are best employed. Prices are signals which reflect a volume of information about wants and costs too great for any central planning agency to comprehend. The market signals tell entrepreneurs what to produce. Anything that interferes with these signals, such as price controls, distorts the messages the market is trying to convey, and the result is misinterpretation and an imbalance of supply and demand which causes unemployment.

For Prof. Hayek the chief villains of the contemporary British scene are the trade unions. Not only are they incapable of affecting the general level of wages (gains for one group of workers being secured at the expense of other groups of workers) but their ability to raise the price of their members' labour actually creates unemployment. When demand for one product increases while that for another declines, there should be a transfer of labour from firms making the less popular product to those making the more popular one, but all too often the workers in the firm whose business is expanding cream off most of the benefits for themselves by restricting the entry of new workers. For this reason, Prof. Hayek asserts that there will be no salvation for Britain until the legal privileges of

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F. A. Hayek, 1980s *Unemployment and the Unions*. The Institute of Economic Affairs, Hobart Paper 87.

By Bert Brookes

trade unions are removed and relative wages, like other prices, are open to continued change.

Hayek declares that it was the rigidity of the wage structure maintained by the trade unions which drove Keynes to advocate the reduction of real wages by inflation, but argues that as the effect of inflation is to defer the necessary adjustments it can be effective only if applied at an accelerating rate. Potential unemployment piles up as inflation proceeds and becomes evident as soon as inflation stops or slackens, as eventually it must. Hayek believes that attempts to reduce inflation gradually will fail, because the painful symptoms as the drug is withdrawn will last too long to be politically acceptable. He thinks it

should be stopped dead since we will more readily bear severe pain for a short time than lesser pain for longer.

Supporters of the market economy will share Hayek's enthusiasm to set it free, but the attitude of trade unions is not the only obstruction. Inflation is the responsibility of governments: they alone practise it and they alone can stop it, if they have the will to do so.

Among the most interesting of Hayek's remarks are those about the amorality of the market signalling system. The market is frequently criticised because its decrees do not accord with ideas of social justice. Hayek suggests that the market is primarily concerned with communicating what is to be done rather than with rewarding what has already been done and that it therefore has nothing to do with fairness (which in any event is a subjective matter) but is simply a neutral mechanism. Fascinatingly, Hayek contends that the moral instincts we have inherited from a face-to-face society—when buyers and sellers dealt with one another directly—are a hindrance today when people have to adjust to the wishes of others whom they will never see and who are utterly remote from them.

It is a valid point that we must not foul up the market by misguided altruism, but in his eagerness to protect the market Hayek dismisses the moral instincts (apart from honesty) as no more than primitive feelings we ought to have outgrown. One of the virtues of the market is surely that it does not preclude, but happily accepts, private conduct and forms of social organization that go beyond self-interest. Co-operatives and charities, personal giving as well as personal eccentricity, can flourish under capitalism in a way that free enterprise cannot do under socialism.

Prof. Hayek does not ask why poverty may persist even when there is no interference with market signalling. If production is buoyant but the needs of millions of people are not being met, there is something radically wrong with the environment in which the market mechanism is operating. It is this that leads to a sense of injustice and this that must be investigated and put right if a really free international market is to be established.