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Socialism's Fatal Conceit

by Ralph R. Reiland

The appeal of socialism, wrote Nobel-winning economist F. A. Hayek, “depends on the instinctual appeal of promised consequences.”

The problem, argued Hayek, is that “socialism cannot possibly do what it promises.”

Socialism fails, unavoidably, because it is based on the flawed concept, the “fatal conceit,” that one man or one group, one cabinet of commanding officials or one central committee, or one team of planners from Harvard and Yale, can gather and understand enough information in order to reshape the world around them according to their wishes, reshape human nature, and design an economic system that can outstrip the overall and long run performance of the decentralized and basically self-ordering and spontaneous processes of the marketplace.

Prior to the “economic failure of Eastern European socialism, it was widely thought” that “a centrally planned economy would deliver not only ‘social justice’ but also a more efficient use of economic resources,” explains Hayek. “This notion appears eminently sensible at first glance. But it proves to overlook the fact that the totality of resources that one could employ in such a plan is simply not knowable to anyone, and therefore can hardly be centrally controlled.”

That’s why the results of the “plan” seldom work out as its intellectual and political leaders intended. It’s why what starts out as idealism often ends up as disillusion, and then tyranny. As evidence, Hayek points to “a seemingly endless string of ‘utopias,’” i.e., failed systems with unintended consequences on a massive scale, “the Soviet Union, then Cuba, China, Yugoslavia, Vietnam, Tanzania, Nicaragua.”

Here in the United States, it’s exactly the same two flaws that Hayek warned of, i.e., lack of knowledge and conceit, that are simultaneously present in our political leadership and got the ball rolling to produce our current economic crisis.

“Congress and regulators pushed Fannie Mae and Freddie Mac to become a vast duopoly in the mortgage finance industry,” writes David Boaz, executive vice president of the Cato Institute and author of *Libertarianism: A Primer*. “Their debt was implicitly backed by the Treasury Department, and they were able to expand their debt and engage in risky transactions.”

With big bonuses to be made at Fannie Mae and Freddie Mac for increased volume and the government, i.e., the taxpayers, standing by to pick up any losses, the stage was set for some top level central planning and high-priced social engineering.

As Larry Summers, Obama's chief economic advisor, explained, "Little wonder with gains privatized and losses socialized that the enterprises have gambled their way into financial catastrophe."

The central plan for housing? No money down, more homeowners, more happy voters, all by way of cheap mortgages and rising house prices.

"There was substantial agreement in Washington that homeownership was a good thing and that more homeownership would be even better," writes Boaz. "Thus Congress and regulators encouraged Fannie, Freddie, and mortgage lenders to extend credit to under-qualified borrowers. To generate more mortgage lending to low- and moderate-income people, the federal government loosened down-payment standards, pressured lenders to increase their percentages of 'affordable' loans, and implicitly guaranteed Fannie and Freddie's dramatic expansion."

The result was a flood of non-prime mortgages, a corresponding surge of bad loans, the development of convoluted financial products to finance and redistribute the substandard paper, rising home prices and an inevitably bursting bubble.

"In 1996, the department of Housing and Urban Development gave Fannie and Freddie an explicit target: 12 percent of their mortgage financing had to go to borrowers with incomes less than 60 percent of their area's median income," reports Anna J. Schwartz at the National Bureau of Economic Research. "That number was increased to 20 percent in 2000 and 22 percent in 2005. The 2008 goal was to be 28 percent. Between 2000 and 2005, Freddie and Fannie met those goals every year."

Everything went according to plan, in other words, except that our collective nest eggs in the market dropped by \$10 trillion over the past 17 months and the politicians are handing out trillions that they're borrowing from China or pilfering from our kids and grandchildren.

As Hayek explained, central plans go haywire with unforeseen and unintended consequences because everything isn't knowable to the central planners. In other words, they don't know what they're doing.

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