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Summary: The Use of Knowledge in Society

In his paper “The Use of Knowledge in Society” published in The American Economic Review, F. A. Hayek writes to counter the argument that a central planner or board of planners could efficiently allocate resources within an economy. Hayek begins his argument by acknowledging that the support for a central planner stems from the economic calculus and the assumptions used to solve economic models. Namely, the assumption that economic agents poses all relevant information, a given set of preferences and are aware of all means of production.

The fundamental problem laid out by Hayek is that the knowledge necessary to formulate an economic order never exists in a concentrated form, but rather, is scattered to each agent of the economy as incomplete and often contradictory information. Therefore, the goal is to find the best way of utilizing this information to form economic policy and institutions, and to the disagreement of many economists, decide who should be doing this planning. The term planning in economics is often used synonymously with the idea of central planning, which lies on the far end of the spectrum of economic structures. However, planning can be expounded to mean the set of decisions that define an economies allocation of available resources which can include the other end of the structure spectrum; competition, or “decentralized planning.”

The dispersion of knowledge in society can be agreed upon by economists at either end of the planning spectrum, yet the problem arises when you ask the value of different information and the cost of obtaining information. Proponents of central planning claim that transferable knowledge can be passed to an expert or group of experts and used to efficiently allocate the resources of the economy. Hayek argues that these experts overvalue statistical aggregations that show greater stability than the actual movements of the economy in detail because the actual number of elements is not large enough to drive spurious stability without deliberate adjustments. Hence, the value of the “man on the spot,” or the individual who is so immersed in a specific task time and place that their knowledge gives them a particular advantage over everyone else.

Particular knowledge about a unique shipping route or excess of supplies in one warehouse may not seem like enough information to dictate a market allocation, but each individual must only be aware of the relative availability of goods which he uses and the relative value of each good. If the value of goods can be translated in to a numerical index, then economic agents only need to consider this index to adjust quantities and does not need to understand the system as a whole. In this way prices can act as a mechanism to coordinate actions of individuals by communicating information from each “man on the spot.” Therefore, the price system can deliver a single market price similar to how a theoretical central planner would allocate an economy.