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Austrian economics is often caricatured and criticized because of its approach, or deliberate lack of an approach, to mathematical models, multivariable calculus, and econometrics. Attacks are leveled against Austrians such as Mises, Rothbard, and Kirzner for their failure or refusal to avail themselves of applied empirical research in their scholarship. The Austrian methodology most frequently targeted is praxeology.

It is not the purpose of this short article to refute these attacks or to explore their errors and merits. That has been done ably by others (see, for example, the series of debate-essays available here, here, here, and here). Nor does this article attempt to stand up for the deductive reasoning of praxeology or to defend its claims about *a priori* truths, a task better suited for a lengthy work of scholarship, not a short article. This piece instead asks one simple question: does Hayek's early work on trade-cycle theory complicate stereotypes about the methods of Austrian economics or clarify the manner in which Austrians can and do approach economic theory? The answer, of course, is yes.

Hayek proposed that the purpose and function of trade cycle theory was strictly limited: it was "to explain how certain prices are determined" and "to state their influence on production and consumption." Expanding trade cycle theory beyond that purpose and function was, he believed, fallacious. "Any attempt to forecast the trend of economic development," he claimed, "or to influence it by measures based on an examination of existing conditions, must presuppose certain quite definite conceptions as to the necessary course of economic phenomena." But economic development — and the trade cycle in particular — is too important and complex to be guided by mere suppositions regarding matters about which there is much disagreement.

That is precisely what was happening in the 1920s when statistical designs and methods were growing in popularity and replacing general equilibrium theory, away from which Hayek himself moved later in his career. Economists at this time were beginning to treat statistics as conditions or proxies for theory (and even as theories unto themselves) rather than as mechanisms for testing and verifying established theories such as basic deductive inference or feature-by-feature comparison of the natural rate of interest (i.e., "equilibrium") with the existing market rate.

According to Hayek, empirical research either affirms or discredits given methodologies but does not introduce new theories to explain fluctuating trade cycles. Amassing statistics, he maintained, is not the same as adducing or formulating economic laws. Statistics are nevertheless useful because, he explains, “there can be no doubt that trade cycle theory can only gain full practical importance through exact measurement of the actual course of the phenomena it describes.” Statistics, however, will not cultivate theoretical excellence of a kind that should direct trade-cycle theory or the policies that flow from it.

Statistics are useful in the negative sense: they disprove and discredit theories rather than affirm or prove them. They are corroborative but not ultimate guides; they are useful only to the extent that they enable us to make accurate predictions about future conditions, e.g., “to infer from the comparative movements of certain prices and quantities an imminent change in the direction of those movements.” Once statistics are gathered, a theory must be extracted from them--they create inferences to be studied and aggregated, not comprehensive theories to be canonized. That is why Hayek declares that the “value of statistical research depends primarily upon the soundness of the theoretical conceptions on which it is based.” Statistics can be made to prove different points, but only a theoretically sound approach to classifying and elucidating statistics will bring about reliable forecasts.

Correct business forecasting depends on correct theorizing; therefore, Hayek propounds, we must labor to attain correct theories, never settling with what we perceive to be complete knowledge. Traditional equilibrium theory is not enough for him because it does not adequately account for money, a commodity or medium of exchange whose very status as such depends on its wide use and general acceptance on the market, not to mention its ability to reflect the subjective values of producers and consumers. The production of money and the often arbitrary increase in its supply by banks distort the natural interest rate and call into question the usefulness of equilibrium theory in a money economy.

Hayek demonstrates in his early work on the trade cycle that statistics and theories can be interactive and participatory so long as the former isn’t treated as a substitute for the latter. Statistics alone aren’t pure math, of course, and the creation of economic simulacra in the form of models and diagrams can lead to the type of scientism — the privileging of data over theory — that Hayek decries. *Math* is a term for what is done with data already gathered; it refers to many topics of study but in this context to the deductive and systematic study of facts and figures and their observable patterns to arrive at true concepts and accurate measurements regarding the concrete conditions of our phenomenal world. So understood, math is not the *ultima ratio* but an indispensable tool, not an end but a means to an end. Only from this premise does Hayek’s trade-cycle theory become fully comprehensible, and although his paradigms of trade-cycle theory and equilibrium evolved over time, his foundational approach to the role of statistics and theories remained crucial to his thinking.

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Note: Quotations come from F.A. Hayek, *Prices and Production and Other Works: F.A. Hayek on Money, the Business Cycle, and the Gold Standard*. Edited with an Introduction by Joseph T. Salerno. Auburn, Alabama: Ludwig von Mises Institute, 2008.

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Tags: Friedrich Hayek, statistics, trade-cycle theory

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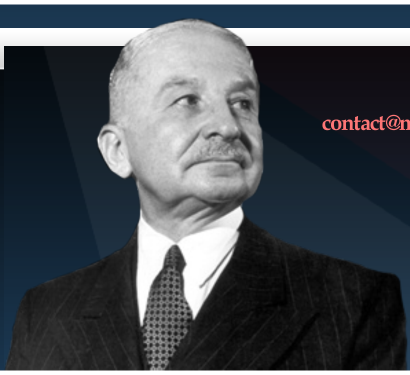

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