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## **Hayek on economic and civil liberty**

### **A critical reflection on *The Road to Serfdom* (1944)**

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## 1. Introduction

Born in 1899 in Vienna, then the capital of the Austrian-Hungarian empire, Friedrich August Hayek turned out to be an important liberal thinker of the 20<sup>th</sup> century during his career as economist and political philosopher. Being laureated with a Nobel Prize in 1974 for his work in the theory of money and business cycles, he has been widely regarded as a leader of the Austrian school of economic thought. His less scholarly book *The Road to Serfdom* (1944) became a best seller near the end of the Second World War, in which he made a case against collectivism of all forms. By interpreting this argument and finding the philosophical foundations and relations connected to Hayek's ideas this thesis will aim to reflect on *The Road to Serfdom*.

In the book, Hayek argued that Nazi Germany and the Soviet Union should be a warning to all liberal nations, because state control of the economy would inevitably end in the destruction of the freedom of the individual. Their development was very much at odds with Hayek's plea for individualism and economic liberty to preserve political freedom. He points out that the promise of freedom by (national) socialism was in fact false and would ultimately lead to the opposite: serfdom. Hayek warned that Western democracies were on their way down the road to serfdom, since in countries like Great Britain he noticed, even at the end of the war, the same intellectual tendencies that in Germany had led to National Socialism. Fundamentally, he argues that there can be no political liberalism without economic liberalism. Socialism – if it implies central economic planning – is therefore irreconcilable with individual freedom. To further explore Hayek's argument, the research question of this thesis is formulated as follows.

Research question:

Why did Hayek think that central economic planning would inevitably lead to tyranny?

For the purpose of answering the research question, this thesis is structured as follows. In chapter 2, *The argument of The Road to Serfdom (1944)*, the line of reasoning contained in Hayek's book will be presented. Since Hayek's ideas have been often misunderstood over the years,<sup>1</sup> a representation of his argumentation will be given

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<sup>1</sup> Boettke & O'Donnell, "The failed appropriation of FA Hayek by formalist economics."

chapter by chapter to make Hayek's logic as clear as possible. This is done by focusing on the first eleven chapters of *The Road to Serfdom*, which are most relevant for the purpose of this thesis, although some reference will be made to the remaining chapters of the book as well. In this way, the essential building blocks are provided to address the research question at hand. In chapter 3, *Philosophical axioms of Hayek*, Hayek's philosophy will be analysed and discussed, mainly revolving around Hayek's conception of liberty and how it connects to other thinkers. In chapter 4, *History of ideas*, the history of Hayek's ideas concerning socialism and central economic planning will be investigated. Finally, in chapter 5, *Conclusion*, the thesis will be concluded by discussing the case of China and arguing for the contemporary (metaphysical) relevance of Hayek's work.

## **2. The argument of *The Road to Serfdom* (1944)**

Hayek starts out with a historical sketch of Western civilization (Chapter 1), after which he investigates the roots of socialism (Chapter 2). Next, he defines the term central economic planning (Chapter 3) to then systematically criticize its different aspects on philosophical, political, economic and moral grounds (Chapters 4-11).

### **I. The Abandoned Road**

According to Hayek, economic freedom has historically been a prerequisite for personal and political freedom, since the transformation of a hierarchical feudal society to a liberal one is associated with the growth of commerce, e.g. as seen in 16<sup>th</sup> and 17<sup>th</sup> century Britain, the Netherlands and northern Italy. Built on principal elements of ancient philosophy and Christianity, above all the West developed into an individualist civilization during the Renaissance. Respect for the individual thus became an intrinsic characteristic of Western civilization. Hayek observed, however, a slowing down in the progress of liberalism, which was accompanied by a departure from the basic ideas on which Western civilization has been built. Belief in liberalism faded, while the laborious achievements of it were taken for granted. It was thought that only a complete remodeling of society could provide further improvements, which notion paved the way for the revolutionary socialist ideologies of communism and fascism. The push for reorganisation of society mainly came from the German intellectuals who resisted the ideas still held up to the west of the Rhine: liberalism and democracy, capitalism and individualism, free trade and internationalism. Under this influence, the Western attitude towards society changed gradually and by almost imperceptible steps, but the cumulative effect of it had nonetheless brought about a radical shift already in Hayek's time. This change meant the abandonment of the individualist tradition fundamental to Western civilization.

### **II. The Great Utopia**

With the knowledge of how traditional Western civilization is seemingly declining, Hayek describes the origins and false promises of socialism, the methods of which he views as the root cause of this decline. Socialism has its foundations as a reaction to the liberalism of the French Revolution of 1789. Early French socialist thinkers were authoritarians who believed that their ideas could only be implemented by a strong dictatorial government, then with the purpose of terminating the revolution. They

regarded freedom of thought as evil. French philosopher Alexis de Tocqueville already realised that socialism is irreconcilable with democracy as an essentially individualist institution. Only later around 1848 “democratic socialism” nevertheless arose. Socialism views political freedom (i.e. democracy) only as the first stage of emancipation and promises “new freedom” which would liberate the people from the restraints of the economic system. Freedom in this new sense is merely another name for power or wealth, of which equal distribution is demanded just like before. The perspective that the new tyrannies of fascism and communism represent opposite poles is a common misconception, when they were in fact the outcome of the same socialist tendencies. And it turns out that the Road to Freedom as promised by socialism is in fact the High Road to Servitude. Democratic socialism is the great utopia: while it is unachievable, to strive for it produces the opposite of the freedom it promises, tyranny.

### **III. Individualism and Collectivism**

After this introduction to socialism, Hayek juxtaposes it with liberalism to assess their respective (economic) characteristics. On the one hand, socialism expresses as its ultimate aims the ideals of social justice, greater equality, and security. On the other hand, socialism also provides the method to hypothetically attain these ideals: by abolishing private enterprise and private ownership of the means of production, and creating a system of “planned economy” in which the entrepreneur working for profit is replaced by a central planning body. Hayek makes clear that the book deals with the consequences that follow from the methods of collectivism, regardless of which ends were aimed at. Socialism is the most important species of collectivism, although collectivism includes all types of planned economy. The term “central economic planning” is defined, because the word *planning* has been usurped by socialists to mean something different than before. In this context, two types of political planning can be distinguished: one where government restrains itself to creating the best conditions under which individuals can plan most successfully (liberalism) and the other where allocation of resources requires central direction in a society consciously organized by the government (socialism). Economic liberalism does not argue for *laissez-faire*, but for organizing society in such a way as to make best possible use of the forces of competition, which is no argument for leaving things just as they are. It even emphasizes the importance of a carefully thought-out legal framework for

competition to work effectively and beneficially. Competition is regarded as a superior mechanism (over central planning) because it is the most efficient method known to coordinate human efforts, even more so because it is the only mechanism without coercive or arbitrary intervention of authority. It is pointed out that the argument of the book only criticizes the socialistic “planning *against* competition,” whereas economic liberalism is in favour of “planning *for* competition”.

#### **IV. The “Inevitability” of Planning**

To further explain the benefits of competition, Hayek discusses the downsides of anti-competitive tendencies and argues against their historical inevitability. In Hayek’s time society had seen the decline of competition and the growth of monopoly manifest itself in the economic order. As a response to these developments, planners asserted that central economic planning had become inevitable. Monopoly was thought by them to have resulted from technological developments as a necessary product of the evolution of “capitalism.” Following the Marxist doctrine of “concentration of industry,” planners then sketched a false dilemma between control of production by private monopolies and central economic planning by the government. Hayek argues that the progressive growth of monopolies has not been an inevitable consequence of technological development, but rather the result of the policies pursued in most countries. First, Hayek explains that optimal economies of scale are reached long before a monopoly or oligopoly is formed in the market, debunking the notion that firms will achieve ever decreasing costs per unit by increasing the scale of production up to levels of full market control. In fact, monopoly is often attained through collusive agreement or promoted by public policies, and not because of lower costs of greater size. Second, Hayek shows that “monopoly capitalism” arose as a consequence of deliberate policy to suppress competition. Germany – as a prime example of where “conscious organisation of industry” had taken place – had been subduing the competitive system by deliberately fostering the growth of cartels and syndicates since 1878. Furthermore, Hayek addresses the misunderstanding that modern industrial civilization becomes too complex for competition to deal with and therefore we must resort to planning. To take into account all market information in a planning system, decentralization into governing agencies becomes necessary, between which there can be no perfect coordination to balance all decisions of the many individuals within that market. Under competition, however, the combination of decentralization and



automatic coordination is achieved by the price system, enabling producers to adapt themselves accordingly to supply and demand within a given market.

## **V. Planning and Democracy**

After pointing out these economic and technical faults of central planning, Hayek discusses its incompatibility with democracy by arguing for moral pluralism. He argues that conscious direction of economic activity towards an ultimate social goal by following a unitary plan does not work, because no complete ethical code of human values exists to guide such decisions. People's views on moral questions would either be indefinite or conflicting, which makes the deliberate organization of the labours of society towards a single aim impossible. The philosophy of individualism is based on the fact that – if attempting to form an all-inclusive scale of values – no individual can comprehend the infinite variety of different needs of different people. Individuals should be allowed, within defined limits, to follow their own values and preferences. Common “social ends” can be pursued if they are coinciding individual ends, i.e. the identical ends of many individuals, or ends for which there is a willingness to contribute in return for something else. Common political action is only possible when people agree on such common ends. Most often these are not ultimate ends, but means by which people can pursue a variety of purposes. Therefore, democracy can only exist where the political scope is restricted to themes where true agreement is reached, and other political themes are left to chance. There can be no democratic majority agreement on a central economic plan, because the economic problem essentially involves choosing between conflicting or competing preferences of different people. The largest possible group that would realistically be able to reach consensus may still be a small minority, which would then impose its will on the rest of the people. The consequent necessity of delegating the act of planning to an expert inevitably leads to the projection of the expert's preferences on the community for which they plan. Even without central planning, when the proportion of the economy under state control exceeds more than half of national income, the remaining part of the economy is almost unavoidably affected by the state's decisions. As a consequence, the state would indirectly control nearly the whole economy, including practically all individual ends, as was the case in Germany in 1928 when government authorities directly controlled the use of 53 percent of national income. Therefore, economic dependence on government to such an extent is undesirable in a democracy as well.

## **VI. Planning and the Rule of Law**

Closely connected to the concept of democracy is the idea of the Rule of Law, the political implications of which Hayek compares to those of central economic planning. Hayek elaborates on the distinction between the creation of a permanent legal framework within which the productive activity is guided by individual decisions and the direction of economic activity by a central authority. In more general terms, this is the contrast between the Rule of Law and arbitrary government respectively. Under the Rule of Law, government restricts itself to creating the ex ante conditions for the use of resources, so that individuals in turn may decide for what ends these resources are used. This type of polity depends on *formal rules* that are drawn up in advance and which are instrumental to the people's individual pursuits. This way any coercive action of the government becomes predictable; the rules of the game become clear. Under arbitrary government, however, resources are directed to particular ends by the government itself, which process cannot rely on formal principles but instead requires *substantial rules* that are set on a case to case basis, leading to deliberate economic choices that are unpredictable in any formal sense. Such planning necessarily involves discriminating between particular needs of different people. Government must then decide how well off particular people shall be and what people are allowed to have and do. This means a return to the rule of status and privilege, reversing the progressive movement of societies to the rule of contract. The Rule of Law – which safeguards equality before the law – is the embodiment of freedom and therefore the true opposite of arbitrary government. State interference in a *Rechtsstaat* must be in accordance with liberal principles, which amounts to governmental action foreseeable by the individual, based on general and permanent rules.

## **VII. Economic Control and Totalitarianism**

After associating central economic planning with arbitrary government, Hayek further argues why a state with a directed economy is necessarily dictatorial. Planners will defend a dictatorship by stating that the authority's mandate will only stretch over economic matters. This argument assumes that economic aspects of life are of lesser importance. And when the supposedly inferior task of addressing the economic problem is delegated to a central planner, the people would be relieved to pursue higher values and obtain greater freedom. However, a more accurate characterization

of the economic motive would be “the desire for general opportunity, the desire for power to achieve unspecified ends.” In the latter context, money facilitates freedom, because it enables people to freely choose which benefits to acquire to satisfy their needs and desires. As long as people can freely dispose over their wealth and income, a merely economic loss (or gain) would therefore constitute a loss (or gain) only in the margin. This is to say that people who are free to allocate their resources will always cut back on the least important needs first when restricted. By contrast, the authority that controls all economic activity controls the means for all ends, and leaves no real free choice over resource allocation to the individual. The crux is that the central planning authority consequently decides which ends are to be satisfied and which not, and thereby ultimately what men should believe and strive for. In short, the state gaining full economic control via central planning leads to totalitarianism. A society in which the availability of jobs, goods and services is planned by a central authority is not free, but at the mercy of the most powerful monopolist conceivable.

### **VIII. Who, Whom?**

Following on from the previous chapter, Hayek examines the problem of deciding on the range of central economic planning. Considering the close interdependence of all economic phenomena, when engaged in the act of planning it is impossible to decide on the exact scope of the state’s economic control. Once free market forces are impeded beyond a certain level, the central planner is forced to increasingly extend its control until it becomes totalitarian. With this tendency the social position of the individual will be less decided by impersonal factors (of the free market) and more by deliberate decisions (of a central authority). Therefore, resentment about inequality would be worse in a planned state, as economic disparity imposed by design affects the dignity of the individual much more. Moreover, improving one’s position will then depend on gaining the authority’s favour instead of preparation for uncontrollable circumstances. The key political issue of a planned state revolves around the question of who plans, directs and dominates whom? Consequently any governmental action will have some effect on “who gets what, when and how.” Two fundamental distinctions are made: the first considers whether the state knowingly and willingly aims its measures against certain individuals or if the resulting effects of its activities are unknowable, the second considers whether the state decides on everything that anyone gets at any time or just on some things some people get in some way at some time. In the latter context, a

conscious ordering of all social relations requires the general acceptance of a common *Weltanschauung*, which encompasses a definitive set of values. The larger and more heterogeneous a group is, the harder it is to arrive at a common world view, and the more likely this will lead to a clash of particular interests groups. It is indeed the case that Fascism and National Socialism grew out of disappointment of the fact that international socialism merely had furthered the interest of a particular class. Nevertheless, each of these socialist movements agreed on the desirability of the state controlling all economic activity.

### **IX. Security and Freedom**

Having made clear the main political issues associated with planning, Hayek covers its employment aspects in this chapter. Hayek contrasts limited security with absolute security, which terms signify a minimum of sustenance and a minimum income respectively. Limited social security and insurance, as well as communal action in case of disaster or emergency, are compatible with liberal principles in a competitive society. Furthermore, the mitigation of general fluctuations of economic activity and unemployment waves may be achieved through planning for competition and sound monetary policy, but Hayek warns for the anti-competitive effects of Keynesian demand management policies in the form of government expenditure towards public works. Although the latter policies are not of the dangerous kind of planning, it should be avoided that all economic activity becomes progressively more dependent on the direction and volume of public spending. What does pose a threat to freedom, however, is absolute security (i.e. certainty of income), which can only be given to all in a situation without free choice of occupation. And if such a privilege is to be given only to some people, it will come at the expense of others whose security is thereby necessarily diminished. Moreover, by introducing a guaranteed income, the height of remuneration gets disconnected from a person's actual usefulness. Consequently, if changes in the employment distribution cannot be influenced by pecuniary incentives, they must come about by direct orders. In its ultimate form, this manner of social organization constitutes a military type of society, e.g. ancient Sparta or Nazi Germany, which is opposed to a commercial type of society. All in all, the fundamental issue is the trade-off between security and freedom. In a market system security can be given to particular interest groups through restrictive measures tolerated or supported by the state, which limit the output quantities within a certain market in

order to stabilize profits or wages. Restrictionism thus fixes the natural instability of prices and wages, but in turn causes heavy fluctuations in employment and production levels. Every such grant of security to one group necessarily reduces the security of the rest. And the great variety of opportunities, which is the type of security offered in a competitive society, is diminished accordingly. With higher insecurity, the greater the contrast between the privileged and the unprivileged. And the more security becomes a privilege, the higher security will be prized – until the social hierarchy will value security over independence and people are prepared to give up their freedom to obtain economic certainty.

## **X. Why the Worst Get on Top**

Now that most economic and political aspects of planning have been addressed, Hayek elucidates how its moral sphere drastically comes to differ from morality in a liberal society. It is commonly misconceived that totalitarian regimes in history turned bad just because they were established and ruled by thugs. There are, however, strong reasons to believe that the bad features of totalitarianism are not accidental, but actually phenomena inherent to such a system. A newly ascended totalitarian dictator would soon face the choice between failing or disregarding ordinary morals. Therefore, the unscrupulous and uninhibited are more likely to thrive under these political conditions. The moral sphere under collectivism thus differs crucially from the essentially individualist Western civilization and will depend on what leads people to success in such a system. In the early stages of any collectivist movement, a numerous and strong group with fairly homogenous views is most likely to be formed by the worst elements of society. This tendency can be explained by three principles of negative selection. First, the largest group of people with similar values consists of those of the lowest common denominator in the sphere of moral standards. Second, the support of the docile and gullible people will be fairly easily won by indoctrination. Third, a skillful demagogue will be able to unite people for common action by arousing the hatred of the in-group (“we”) towards a common enemy (“they”), since it is a bias of human nature that makes it easier for people to agree on something negative. Another limitation of collectivism is its tendency towards particularism, e.g. nationalism, racialism or classism, which has to be accompanied by a common feeling of identification with other members of the particular group. For this reason, world-wide collectivism seems to be unthinkable, except to the benefit of some small ruling elite.

While socialism is supposedly humanitarianist and internationalist in theory, in practice it becomes particularist and violently nationalist. With the goal of implementing a central planning system, it is the desire for power that ultimately drives collectivists. And the amount of power wielded by a central planning board is infinitely greater than the sum of the power of all private boards of directors. Conversely, the competitive system guarantees individual freedom by separation of political and economic aims and minimizes the (economic) power exercised by man over man via decentralization. While the rules in individualistic ethics are general and absolute, which can be freely applied by the individual conscience, the supreme rule in collectivistic ethics is the principle that the end justifies the means, as long as it serves “the good of the whole.” Therefore, leading positions in a totalitarian system will be special opportunities for the ruthless and unscrupulous – who are prepared to do bad things without the constraints of traditional morals.

## **XI. The End of Truth**

After sketching the moral sphere that is thought to be inherent to totalitarian regimes, Hayek assesses the metaphysical nature of totalitarianism. Totalitarian propaganda does not merely change the people’s moral code, but actually destroys one of the foundations of all morals: the sense of and the respect for truth. This is because in a collectivist society the people must not only agree on the ultimate ends, but also on the facts on which the means to reach those are based. An effective way in which this has been done, is the perversion of language which causes words like “freedom”, “justice”, and “equality” to mean the opposite of their original denotation, while they are used solely for the purpose of evoking the still adherent emotional associations. The great majority of people can be deprived of independent thought fairly easily, but the minority who will remain inclined to criticize must also be silenced. To retain public support in a collectivist state, every act of the government must become exempt from criticism. All information spread by enterprise, media, and science must be in service of the authorities, as to strengthen the belief in the rightness of their decisions and thereby the loyalty of the people. This tendency is a direct result of the desire to see everything directed by a “unitary conception of the whole.” It marks the end of “truth” in its original meaning, because truth is no longer something to be found and for which evidence may be judged by the individual conscience. Instead, truth is laid down by authority. Although freedom of thought may in practice be directly relevant only to an

intellectual minority, it is paramount for progress that any cause or idea may be argued by somebody. The growth of reason is a social process thus depending on freedom of thought among interacting individuals who possess different knowledge and different views. The philosophy of individualism recognizes these dynamics with humility and tolerance towards different opinions.

### 3. Philosophical axioms of Hayek

Using the building blocks provided in the previous chapter, Hayek's philosophical axioms are mapped and analysed next on the basis of a set of key general concepts derived from *The Road to Serfdom*. Specifically, Hayek's thoughts on the Rule of Law, liberty, moral pluralism and historical inevitability are related to other philosophers.

#### 3.1 Reflection on general concepts

##### 3.1.1 Philosophical

In *The Road to Serfdom* Hayek's argument is based upon three closely connected key philosophical concepts: individualism, liberty, and progress. The book starts with the claim that individualism is at the foundation of Western civilization. Hayek believed the essence of the individualist position to be the recognition of the individual as the ultimate judge of his ends, who therefore ought to act according to his own views as far as possible.<sup>2</sup> Individuals should be allowed to follow their own values and preferences within defined limits. This entails developing one's own talents in a world of trade and contract, without despotic political power. The individual is sovereign, for he is his own highest authority.<sup>3</sup> But to be sovereign is to be free, and thus the individualist position immediately ties into the liberal position. The nature of and limits to freedom of the individual will be addressed in more detail in paragraph 3.2 *Liberty versus tyranny*. Throughout the book Hayek affirms the aim of achieving true progress. Metaphysically, progress may be characterized as the movement towards the rule of contract (where matters are negotiated and agreed upon), away from the rule of status (where matters are settled on the basis of privilege). Economically, progress would mean the increase of the general level of wealth, or in utilitarianist terms: the increase of utility for the greatest number of people (cf. Hume, Bentham, J.S. Mill). The nature of utility is another complicated matter, but for now it should be sufficient

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<sup>2</sup> Hayek, "Planning and Democracy," in *The Road to Serfdom*, p. 102: "The individuals should be allowed, within defined limits, to follow their own values and preferences rather than somebody else's; that within these spheres the individual's system of ends should be supreme and not subject to any dictation by others. It is this recognition of the individual as the ultimate judge of his ends, the belief that as far as possible his own views ought to govern his actions, that forms the essence of the individualist position."

<sup>3</sup> The idea of the sovereign individual can be found in Mill, *On Liberty*, p. 22: "In the part which merely concerns himself, his independence is, of right, absolute. Over himself, over his own body and mind, the individual is sovereign."



to note that in the field of economics several efficiency criteria have been formulated for evaluating changes in general welfare, e.g. the Pareto and Kaldor-Hicks criteria.

### 3.1.2 Political

Furthermore, two key political concepts are assumed: the Rule of Law and democracy. Hayek characterized the Rule of Law as the embodiment of freedom, and as being essential to freedom. The logical conclusion would therefore be that liberty cannot exist without the Rule of Law, so what does it actually entail? The Rule of Law recognizes the sovereign individual and makes possible the diversity of people by guaranteeing that all individuals will be treated equally before the law, regardless of any physical or social characteristics. The main feature of this political system is that the state does not act arbitrarily. The way this can take shape legally is by formulating permanent formal principles as much as possible, since reliance on formal rules make the outcomes of legal procedures more predictable, as Hayek pointed out.<sup>4</sup> Economically, the predictability provided by permanent formal rules is an important condition for the willingness of entrepreneurs and investors to take risks, and more generally for maintaining well-functioning markets and consumer confidence, since the hypothetical effects of possible governmental actions or any civil disputes then can be taken into account by all market participants reasonably well into the future. From *The Road to Serfdom* it follows that Hayek is under the impression that the Rule of Law has been declining, and attributes this development at least partly to the progressive introduction of vague formulas into the legal framework, which consequently makes the law more arbitrary and uncertain almost by definition, turning it more and more into a policy instrument exercised by the judicial class.<sup>5</sup>

The idea of the Rule of Law, or the Rechtsstaat, can be traced back to the political writings of Kant.<sup>6</sup> Not only did he oppose enlightened autocracy, but also politics viewed as mere exercise of statecraft or based on Machiavellian egotism. Instead, he preferred a state governed according to the Rule of Law, with a liberal outlook. Kant thought that a social contract implying a union as an end in itself, which all individuals ought to share, may be only found in a civil state. What is right is to restrict individual

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<sup>4</sup> Hayek, "Planning and the Rule of Law," in *The Road to Serfdom*, pp. 112-114.

<sup>5</sup> Hayek, "Planning and the Rule of Law," in *The Road to Serfdom*, p. 116.

<sup>6</sup> Reiss, "Introduction," in *Kant: Political Writings*, pp. 11-13.

liberty so that it harmonises with the liberty of all other individuals. A civil state follows from the relationship among free individuals, all subject to coercive laws, while they retain the freedom among themselves. Furthermore, a civil state is lawful based on the following a priori principles with respect to its members: (1) freedom, as a human being, (2) equality, as a subject, and (3) independence, as a citizen.<sup>7</sup> In Kant's view, the civil state should be patriotic instead of paternal, in which each member of society has the authority to protect lawful rights and should not have to rely on the benevolence (or malevolence) of the government. From this follows the individualist position and the notion of limited government, entailing the freedom to choose how to live privately according to one's wishes insofar this is reconcilable with the Rule of Law. The Rechtsstaat is thus a collective framework in which individuals, as well as government, are subject to the law, but may act freely within its boundaries.

Regarding the second political concept, Hayek does not argue explicitly for democracy, although he points out that it cannot exist under central economic planning. This is because the competing preferences of all the different people within society prevent reaching democratic majority agreement on any central economic plan. Instead, planning would lead to the rule of experts to whom this task is necessarily delegated when no consensus can be made. Conversely, democracy can only exist where the scope of political action is restricted to themes where true majority agreement is reached. Implicit in Hayek's thoughts on democracy are the associated civil liberties safeguarded by the Rule of Law – stemming from the ideas of Mill – which prevents Parliament from infringing on fundamental rights or oppressing (political) minorities.<sup>8</sup>

### 3.1.3 Economic

More specifically, Hayek substantiates his philosophical and political arguments against central economic planning (and *for* economic freedom) using the key economic concepts of competition using the price mechanism and marginal utility. Competition is regarded as the superior market mechanism because it is most efficient and least dependent on coercive authority. In a competitive system, it is up to the

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<sup>7</sup> Kant, "Theory and Practice," in *Kant: Political Writings*, p. 74.

<sup>8</sup> Mill, *On Liberty*, pp. 11-14.

individual to decide if the benefits of a particular occupation compensate for the associated disadvantages and risks, and if buying a particular good is worth the price (which is in Hayek’s view assessed subjectively in terms of marginal utility). In other words, ideally, happiness and suffering are priced in automatically by the invisible hand of free market economics: namely the price mechanism, which is the impersonal force governing supply and demand in a given market. In *The Road to Serfdom*, Hayek consequently argues against forces that are distorting the functioning of free markets, such as monopolization (Chapter 4), nepotism (Chapter 8), and absolute security and restrictionism (Chapter 9).<sup>9</sup> Each of these distortions comes down to the favouring or privileging of a particular group over the rest of the market participants (i.e. particularism) and thus a move away from the metaphysical rule of contract. In Chapter 10, Hayek sums up the superiority of the competitive system by stating that it minimizes economic power imbalances among people and that it guarantees individual freedom by separation of economic and political aims.<sup>10</sup> Economic freedom creates conditions for general opportunity and enables the individual pursuit to achieve one’s own ends. In short, the foregoing constitutes the specific argument for the notion that economic freedom is a prerequisite for civil liberty and moreover, that progress of Western civilization depends on the coordination of individual efforts by impersonal forces of the free market (Chapter 14).<sup>11</sup>



Figure 1: A visual interpretation of Hayek’s conceptual framework of political philosophy

### 3.2 Liberty versus tyranny

#### 3.2.1 Mill’s concept of liberty

Influenced by 19<sup>th</sup> century British philosopher and political economist John Stuart Mill, many philosophers have since been greatly attentive to the individualist position, among whom Hayek certainly belongs. To increase our understanding of Hayek’s

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<sup>9</sup> Hayek, “The “Inevitability” of Planning,” “Who, Whom?,” and “Security and Freedom”, in *The Road to Serfdom*.

<sup>10</sup> Hayek, “Why the Worst Get on Top,” in *The Road to Serfdom*.

<sup>11</sup> Hayek, “Material Conditions and Ideal Ends,” in *The Road to Serfdom*.

philosophy, it is useful to turn to Mill's ideas with the questions of why we should pursue the ideal of liberty and what the concept of liberty means? Mill, who was one of the fathers of liberalism, made a case for the value of liberty on utilitarian grounds in his famous work *On Liberty* (1859). He argued that the ability to achieve progress for society rests on the freedom of the individual, which claim is a clear precursor to Hayek's emphasis on the progressive value of the individualist tradition of Western civilization nearly one century later. Liberty in the civil sense has been defined by Mill as "the nature and limits of the power of which can be legitimately exercised by society over the individual."<sup>12</sup> Thus, Mill's concept of liberty is expressed in terms of the space whereto the power of society may not extend. The limits to that power follow from the principle that authority may only coerce individuals – i.e. interfere with individual freedom – in case they inflict damage upon others. The sole end warranting compulsion and control is the self-protection of mankind; interference is therefore not justified by paternalistic or moralistic ends.<sup>13</sup> Mill also believed in the idea of private property as an individual right associated with (intellectual) production and trade, viewing it as a fundamental institution of society.<sup>14</sup> According to Hegel, who seems to make stronger claims than Mill in this respect, a person is not completely free unless he can participate in an external sphere of – among other aspects of the life of the state – private property rights and contractual exchange.<sup>15</sup> Thus, Hayek's argument for economic freedom as a prerequisite for liberty in a complete sense can be traced back to Mill and Hegel, who emphasized the importance of private property not to be interfered with by the state.

In Mill's time, many states were transitioning or 'progressing' from monarchy to democracy. Nevertheless, he foresaw that freedom would be no less at risk under majority rule than under absolute autocracy, because a tyranny of the majority may equally result in minority oppression.<sup>16</sup> Furthermore, Mill qualified freedom of speech as a vital element of liberty, the value of which he defended by pointing out that any displeasing or unpopular opinion actually might be correct and even if that opinion is

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<sup>12</sup> Mill, *On Liberty*, p. 7.

<sup>13</sup> Mill, *On Liberty*, pp. 21-22.

<sup>14</sup> Cf. Mill, *Principles of Political Economy*.

<sup>15</sup> Hegel, *Philosophy of Right*, p. 48.

<sup>16</sup> Mill, *On Liberty*, pp. 11-14.

false its free expression is needed to prevent true beliefs from becoming dogmatic.<sup>17</sup> This argument again ties in with Hayek's stance on freedom of thought as being essential to progress, entailing that any cause or idea should be allowed to be argued by somebody. Since free speech is quintessential to classical liberalism, it is unsurprising that no such freedom exists under final-stage totalitarianism, the phenomenon which Hayek described as the 'end of truth.'<sup>18</sup>

### 3.2.2 Berlin's two concepts of liberty

To further understand Hayek's thoughts on liberty, which were very much in the spirit of Mill's, we will now focus on an important conceptual distinction that was drawn fourteen years after the publication of *The Road to Serfdom*. Philosopher Isaiah Berlin, who was a contemporary of Hayek, distinguished two political senses of liberty: the notions of 'negative' and 'positive' freedom.<sup>19</sup> Following the trace of Mill and others, negative freedom is basically the classical conception of liberty. The negative concept of liberty consists of a free private space, devoid from any public intervention, that is limited by the principle of not doing harm to other people. In general, coercion is said by Berlin to imply "the deliberate interference of other human beings within the area in which I could otherwise act."<sup>20</sup> The area within the boundaries beyond which legitimate coercion may take place constitutes the negative space of liberty, the space of non-interference.

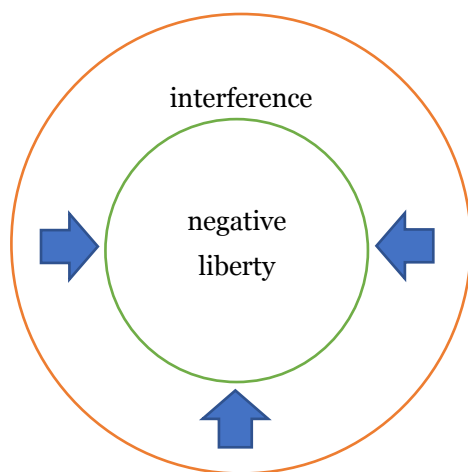


Figure 2: A visual interpretation of the 'negative' concept of liberty

<sup>17</sup> Mill, "Of the Liberty of Thought and Discussion," in *On Liberty*.

<sup>18</sup> Hayek, "The End of Truth," in *The Road to Serfdom*.

<sup>19</sup> Berlin, "Two Concepts of Liberty," in *Liberty*.

<sup>20</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, p. 169.

*Mill's negative liberty =  
the area of all possible action – the area of all possible action harming others*

Berlin criticized Mill on three accounts with the purpose of arriving at his positive concept of liberty.<sup>21</sup> Firstly, Mill claimed that coercion is bad as such, while non-interference is good as such (the negative conception of classical liberty), and that truth can be found only under conditions of freedom. But history shows that liberty is no necessary precondition for either truth-seeking or individualism, for even in severely disciplined societies such endeavours have been observed. Secondly, liberty is a comparatively modern doctrine, a conception of freedom which originated during the Renaissance and Reformation. Domination of the liberal ideal has been the exception, rather than the rule. Thirdly, liberty is not incompatible with some kinds of autocracy like enlightened despotism or with the absence of self-government. In other words, there is no necessary logical connection between individual liberty and democracy. This third criticism leads to the conception of the positive sense of liberty, which asks the question: “By whom am I ruled?”<sup>22</sup> This is logically distinct from the negative sense of liberty, which asks the question: “How far does government interfere with me?” In short, Berlin’s point is that negative liberty may exist in a society that lacks positive liberty. While negative liberty deals with external restraints on individual action, positive liberty considers the degree to which internal restraints affect the autonomy of an individual or group. The tension between the positive sense and the negative sense makes clear that the two concepts of liberty may be incompatible with one another.

### *3.2.3 Kant’s autonomy*

Expressed through the positive sense of liberty is the wish for individual self-mastery. Berlin considered two major forms this desire for self-direction has historically taken.<sup>23</sup> The first has centred around the aim of attaining independence, like in Stoic philosophy or Buddhism.<sup>24</sup> This line of thinking can be found in the work of Kant, who

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<sup>21</sup> Berlin, “Two Concepts of Liberty,” in *Liberty*, pp. 175-178.

<sup>22</sup> Berlin, “Two Concepts of Liberty,” in *Liberty*, p. 177.

<sup>23</sup> Berlin, “Two Concepts of Liberty,” in *Liberty*, p. 181.

<sup>24</sup> Berlin, “Two Concepts of Liberty,” in *Liberty*, pp. 181-187.

identifies freedom with the control of desires.<sup>25</sup> Liberal humanism was influenced by Kant's conception of the free individual as a transcendent rational being, risen above the world of natural causality.<sup>26</sup> He proposed that being autonomous is the essence of man, and that man is free insofar he is autonomous, obedient only to a set of self-imposed rational rules. The individual is the highest value, for all values arise from the free acts of men. This idea is echoed by Hayek when he marks liberty as a prerequisite for moral value, since a personal decision has to be made voluntarily for it to be of moral significance in the first place. The ability to do what one wishes as a definition for Mill's concept of liberty does not suffice when one is able to liberate oneself by simply eliminating any desire. In other words, one could maximize one's freedom in the negative sense plainly by not wanting anything. The alternative to such self-abnegation brings us to the second form of self-direction: an attempt to bend the world to one's wishes, in however a cruel, unjust, or violent way, as history has shown, but which may actually result in increasing one's own freedom in the positive sense.

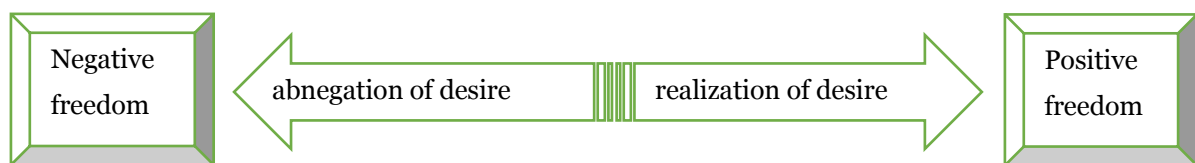


Figure 3: A visual interpretation of the abnegation-realization spectrum

### 3.2.4 Failure of the rationalist argument

The metaphysical foundation of positive freedom lies in the concepts of rationality and self-realization.<sup>27</sup> To understand the world is to be freed, thought Herder, Hegel, and Marx. The idea that knowledge liberates us from the frustration of attempting the impossible is at the metaphysical foundation of rationalism. The positive doctrine of liberation by reason is based on Marx's idea of institutional oppression. This derives from the Hegelian idea of dialectical conflict and the notion of rationally intelligible laws governing social institutions. Berlin demonstrated how the rationalist argument for freedom leads from individualism to authoritarianism.<sup>28</sup> Ideally, autonomy goes hand to hand with authority: liberty governed by law. But how would we be able to

<sup>25</sup> Cf. Kant, *Groundwork for the Metaphysics of Morals*.

<sup>26</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, pp. 184-185.

<sup>27</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, pp. 187-191.

<sup>28</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, pp. 191-200.

constitute the law? Figures like Fichte believed, according to Berlin, in the existence of a single true solution to moral and political problems. They justified compulsion by a rational elite with the purpose of educating the irrational lower elements of society.<sup>29</sup> What started with the Kantian idea of the autonomous and rational individual transformed into the ideal of a society ruled by experts. If maintaining the adage that organization by rationality will set you free, it turns out that despotism by some elite miraculously equates with freedom. To address this contradiction, Berlin argued that actually none of the basic assumptions of the rationalist argument are demonstrable, which are listed as follows: (1) there is one true universal purpose of rational self-direction, (2) the ends of all rational beings necessarily and harmoniously fit into a single universal code, which some people are more apt to discover than others, (3) all conflict is due to the irrational elements in life and therefore in principle avoidable, and (4) when all people are made rational, they are at the same time free as well as governed by their own coinciding rational laws.<sup>30</sup> Based on this critique, he believed the Western tradition of regarding knowledge as virtuous and liberating may be incorrect.

In the context of positive liberty, a connection can be made to Hayek's remark on the "new" freedom promised by socialism, which he viewed as a sleight of hand to cover the lust for power and wealth.<sup>31</sup> Thus, although Hayek does not acknowledge distributive justice as a form of freedom, his liberal position does prescribe creating the best possible conditions for positive liberty in the sense that individuals should be able to empower their creativity to the benefit and progress of society.<sup>32</sup> All in all, a clear parallel can be drawn between Berlin's critique of rationalism and Hayek's critique on the rule of experts and the "scientific" organisation of society.<sup>33</sup>

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<sup>29</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, p. 196, after mentioning Fichte: "Compulsion is justified by education for future insight.' The reason within me, if it is to triumph, must eliminate and suppress my 'lower' instincts, my passions and desires, which render me a slave; similarly (the fatal transition from individual to social concepts is almost imperceptible) the higher elements in society – the better educated, the more rational, those who 'possess the highest insight of their time and people' – may exercise compulsion to rationalize the irrational section of society."

<sup>30</sup> Berlin, "Two Concepts of Liberty," in *Liberty*, p. 200.

<sup>31</sup> Hayek, "The Great Utopia," in *The Road to Serfdom*.

<sup>32</sup> Hayek, "Conclusion," in *The Road to Serfdom*.

<sup>33</sup> Hayek, "Planning and Democracy" and "The Totalitarians in Our Midst," in *The Road to Serfdom*.



### 3.2.5 *The rise of tyranny*

Now that we have reflected on the different conceptualisations of liberty, it may be useful to our understanding to contrast it with its opposite: tyranny. Although tyranny is broadly associated with unpleasant forms of autocracy, in its modern form, as totalitarianism, it is especially dangerous. How does tyranny come about, or more precisely formulated for the purpose of this thesis: what are the origins of totalitarianism? Philosopher Hannah Arendt, who was one of the most influential political thinkers of the 20<sup>th</sup> century, dived into exactly this question in her 1951 book *The Origins of Totalitarianism*.<sup>34</sup> Focusing on the two major totalitarian movements of her time, Nazism and Stalinism, she assessed the mechanics of totalitarianism by discussing the role of propaganda and the use of terror. Arendt observed that the rise of these totalitarian regimes was characterized by a transformation of the organic class structure of society to a classless mass of humanity, a mass which may be more easily swayed by demagogic leadership. Where autocrats seek to attain absolute political power and eliminate opposition, totalitarianists go even further by seeking to dominate every aspect of everyone's life and are imperialistic in nature. Loyalty to the regime becomes the highest value, whereas intellectualism, spiritualism and art are seen as the gravest dangers to the totalitarian establishment. Totalitarianism is thus essentially intolerant of different-minded people. Published a couple of years before Arendt's magnum opus, philosopher Karl Popper pointed out the so-called "paradox of tolerance" in his 1945 work *The Open Society and Its Enemies*. He stated that a society that is tolerant towards the intolerant will be eventually taken over by the intolerant, leading to the disappearance of tolerance. With "the open society," Popper meant a society for which the future remains open (as opposed to a "closed" or totalitarian society), thus assuming the absence of deterministic laws governing society and a situation where no particular class decides on the direction of society as a whole. Popper concluded that we should have the right to not tolerate the intolerant, in order to preserve a tolerant society.<sup>35</sup>

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<sup>34</sup> Arendt, *The Origins of Totalitarianism*.

<sup>35</sup> Popper, *The Open Society and Its Enemies*, p. 581.

### 3.3 Moral pluralism versus totalitarianism

To address Hayek's thoughts on moral pluralism, a link can be made to the moral philosophy of Kant. Kant's moral system, as laid out in the *Groundwork for the Metaphysics of Morals* (1785), is built around a set of moral laws in the form of a categorical imperative, which applies universally and necessarily to all rational agents. The categorical imperative requires the notion that moral agents act only in a way that the principle of their will could become a universal law. Derived from this general statement Kant proposed three different formulations of the categorical imperative: (1) the formula of the universal law of nature, (2) the formula of humanity, and (3) the formula of autonomy. Hayek is clearly inspired by the second notion: "act in such a way as to treat humanity, whether in your own person or in that of anyone else, always as an end and never merely as a means."<sup>36</sup> In this sense, in morality, all individuals are ends in themselves and as rational agents possess dignity, an absolute value, whereas other things are ends with a price and exchangeable.

The philosophy of collectivism comes down to the notion that everything and everyone should always be subordinate to one supreme social good. This presents a clear tension with Kant's categorical imperative, because it is impossible to treat a man as an end in himself when he becomes a mere means in the pursuit of a unitary plan for society. The supreme collectivist rule that the end justifies the means also in the case of man is therefore a grave violation of Kant's humanity formula. However, a collectivist may argue with Kant's third formula of the categorical imperative: "the idea of the will of every rational being as a will laying down universal law."<sup>37</sup> This implies the concept of the kingdom of ends, which is the systematic union of all rational agents as lawgiver of their actions and the ends they set. However, according to Hayek such a kingdom of ends will never exist in political and economic life and never will all rational agents accept a central plan, because social life does not obey to unchanging laws as nature does, but given the radical diversity of individuals, even in morality such an agreement will never be reached. Therefore, Kantian ethics notwithstanding its focus on rationality presupposes a negative concept of freedom. Hayek's views on conflicting morals, freedom of speech and individual autonomy to pursue one's own ends clearly

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<sup>36</sup> Kant, *Groundwork for the Metaphysics of Morals*, p. 29.

<sup>37</sup> Kant, *Groundwork for the Metaphysics of Morals*, p. 30.

display the assumption of moral pluralism. It is perhaps this friction between totalitarianism and moral pluralism that is at the core of Hayek's disapproval of central economic planning.

### **3.4 Contra historical inevitability**

An important idea that Hayek criticizes throughout his work is the notion that history is holistic and deterministic, meaning that society as a whole is subject to some sort of historical laws making its course of events inevitable. This school of "historicism" gained traction during the 19<sup>th</sup> century with thinkers like Hegel, Comte, Fichte, and Marx. One of the major criticisms of historicism came from Austrian philosopher Karl Popper in *The Poverty of Historicism*, originally published as a paper in 1936, and later as a book in 1957.<sup>38</sup> Historicism is defined by Popper as "an approach to the social sciences which assumes that historical prediction is their principal aim."<sup>39</sup> Furthermore, he states that "the belief (...) that it is the task of the social sciences to lay bare the law of evolution of society in order to foretell its future (...) might be described as the central historicist doctrine."<sup>40</sup> Among other problems with historicism, Popper identified the impossibility of describing the whole of society (holism), because it would require an infinite list of characteristics, and the impossibility of predicting the future of society with certainty, because individual human action or reaction is also unpredictable with certainty. Moreover, in *The Open Society and Its Enemies* (1945), Popper called out Plato and Marx for being "enemies of the open society."<sup>41</sup> Their historicist positions, which assume the pattern of history to be inevitable and deterministic, would absolve people from democratic responsibility to shape the evolution of society, which could free the way for totalitarianists to come into power.

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<sup>38</sup> Popper, "Historical Note," in *The Poverty of Historicism*.

<sup>39</sup> Popper, *The Poverty of Historicism*, p. 3.

<sup>40</sup> Popper, *The Poverty of Historicism*, pp. 105-106.

<sup>41</sup> Popper, *The Open Society and Its Enemies*.

## 4. History of ideas

In the previous chapter we have discussed Hayek's conception of liberty, which led to his critique of totalitarianism and collectivist regimes. Fundamentally, this critique is directed against the nature of the social sciences at the time and the political ideas of "planning" derived from them, the history of which is discussed in this chapter.

### 4.1 The genealogy of socialism

*The Road to Serfdom* was intended and received as a rather popular work on political economy and the history of socialism, *which would end in 'serfdom,'* whereas a couple of years later Hayek goes more in depth into the history of ideas regarding this subject in his 1952 book *The Counter-Revolution of Science*. According to Hayek, the most fundamental impulse behind socialism was the drive towards 'social engineering,' to be achieved by the conscious 'organization' or 'planning' of society. This socialist utopian way of thinking revolves around the 'cult of organization,' the aspect of which Hayek specifically combats is the deliberate organization and direction of economic activity – i.e. economic planning.

Hayek's view of the history of socialism can be traced back to a series of lectures by French philosopher Saint-Simon given by his friends after his death in 1829-1830, compiled in the text *Doctrine de Saint-Simon: Exposition*, which Hayek regarded as the Old Testament of socialist thought.<sup>42</sup> Not only was Saint-Simon of great influence in France (to Napoleon III), but also in Germany social policy of Bismarck was based on the ideas of German philosopher Ferdinand Lassalle, who in turn was influenced by Saint-Simon at the root (via the works of Louis Blanc, Lorenz von Stein, and Johann Karl Rodbertus). Exploring these roots of socialist thought, Hayek started an intellectual war against constructivism, among which utilitarianism, contractarianism, and legal positivism are classified. All of these movements viewed social institutions as the products of human construction and thus were thought to be able to be re-engineered. By extension, this theme of social engineering that is also found in socialism may well be its fundamental flaw, for it stands diametrically opposed to the philosophy of individualism. With this background knowledge in mind, it is unsurprising that Hayek dedicates *The Road to Serfdom* "to the socialists of all

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<sup>42</sup> Jones, "The Era of Tyrannies: Elie Halévy and Friedrich von Hayek on Socialism," p. 59.

parties”<sup>43</sup> and explicitly addresses the socialist roots of Nazism in chapter 12 of the book.<sup>44</sup> Thus, although he calls out the Marxist tendencies of several intellectuals throughout the book, Hayek’s critique seems to be directed at a deeper anti-liberal root cause driving both the international (e.g. Marxist) and national (e.g. Nazist) socialist movements.

A 2002 article by H.S. Jones tentatively suggests that the essays of French philosopher and social scientist Élie Halévy (posthumously compiled in 1938 in *The Era of Tyrannies*) influenced Hayek’s writing of *The Road to Serfdom*.<sup>45</sup> Halévy was credited with discovering the non-Marxist roots of socialism, but also for highlighting the consequent antinomy within socialist thought: the principle of emancipation as opposed to the principle of organization. The former principle acts in the spirit of the 1789 revolution, while the latter acts as a reaction to the individualistic and liberal elements of it. Considering this antinomy, original socialism was in fact illiberal and undemocratic, being more inclined towards the second principle of hierarchy and organization. Halévy related the tyrannical tendencies of socialism to the early 20<sup>th</sup> century societal and political developments that took place in the theatre of war. For two main reasons, economic and intellectual respectively, Halévy thought that the ‘era of tyrannies’ had begun in 1914 with the First World War. Firstly, the war was associated with increased state control of the economy and the rise of corporatism and syndicalism. Secondly, the war brought about increased state control of thought in the national interest, both negatively (by suppressing dissenting opinions) and positively (by stimulating enthusiasm).

In essence, Halévy identified the origins of socialism as Saint-Simonian, rather than Marxist. This implies that not the Marxist concept of distributive justice, but that of Saint-Simonian conscious planning is central to socialism. Marx’s *Das Kapital* was seen as the culmination of merely the ideological history of socialism, while it marked the starting point of its political history by providing intellectual gunpowder to the socialist movement. Ideologically, Marxism is characterized as the fusion of Hegelian and Saint-Simonian ideas – as a synthesis of German philosophy, French and English

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<sup>43</sup> Hayek, *The Road to Serfdom*, p. 36.

<sup>44</sup> Hayek, “The Socialist Roots of Nazism,” in *The Road to Serfdom*.

<sup>45</sup> Jones, “The Era of Tyrannies: Elie Halévy and Friedrich von Hayek on Socialism.”

socialism, and English political economy – and not as a creation of fundamentally new ideas.<sup>46</sup> The Halévyan origin of Hayek’s view of socialism is reflected in his definition of the ideology, seeing socialism and fascism as two connected systems. In this regard parallels can be drawn with the works of Popper and Arendt, who likewise opposed all types of totalitarian regimes for being all-dominating and intolerant.<sup>47</sup>

#### **4.2 The Austrian school of economic thought**

To understand Hayek’s writings and philosophy, it is useful to put his ideas in the perspective of the historical developments in the field of economics. In 1871 the Austrian school of economic thought, to which Hayek would belong many decades later, was founded by Austrian economist Carl Menger with the publication of *Principles of Economics*.<sup>48</sup> Menger is mainly known for his contributions to the theory of marginalism, which he called the Subjective Theory of Value. Using the concept of marginal utility, he explained how prices are not determined in a cost-based approach, depending on some inherent property of the product or on the labour that went into it, but by the process of individual subjective assessment of the marginal value the good provides to the consumer’s preferences at a given time. The individual is the appropriate unit of analysis. And thus the logic of individual choice provides an important building block for a universally valid economic theory. This new theory also solved Adam Smith’s diamond-water paradox, dealing with the question of why a pound of diamonds is more valuable than a pound of water, although life cannot exist without water but easily without diamonds.<sup>49</sup> The answer lies in the near infinite marginal value of the first few units of water (which are necessary to live), rapidly declining after the consumption of more units of water, but still making all water in total more valuable than all diamonds in total. However, for someone who is not dying of thirst, diamonds have higher marginal utility than water because of scarcity, whereas water is plentiful.

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<sup>46</sup> Jones, “The Era of Tyrannies: Elie Halévy and Friedrich von Hayek on Socialism,” p. 64.

<sup>47</sup> Popper, *The Open Society and Its Enemies*, and Arendt, *The Origins of Totalitarianism*.

<sup>48</sup> Boettke, “Austrian School of Economics,” in *The Concise Encyclopedia of Economics*.

<sup>49</sup> Smith, “Of the Origin and Use of Money,” in *An Inquiry into the Nature and Causes of the Wealth of Nations*.

Over the years, the Austrian school would rival the then mainstream German “historical” school of economic thought. The historical school believed not in universal economic laws, like the English classical economists such as David Hume and Adam Smith did, but rather in using the historicist method for economic science.<sup>50</sup> Interestingly, the early critique of the Austrian school on historicism has been further developed philosophically by Popper many decades later with his rejection of the idea that society is governed by historical laws. Menger’s revival of universal economic theory was viewed by the historical school with some disdain. Actually, calling this new tradition “the Austrian school” was meant in a derogatory manner. The major Austrian economist of the 20<sup>th</sup> century was Ludwig von Mises, of whom Hayek was a student. Many arguments from *The Road to Serfdom* display Austrian economic thought. In chapter 7, for example, Hayek uses the theory of marginalism to argue in favour of the liberty provided by money in pursuit of the economic motive and to argue against totalitarian economic control.<sup>51</sup> Marginal utility differs for different people at different times. The individual is therefore the most suitable judge for allocating his own resources. The solution of freely exchangeable money thus facilitates people in pursuing their own preferences and not somebody else’s, within the constraints of their budgets. The more authority interferes with the individual’s freedom of allocation, the less liberty he has in a broader sense, becoming more dependent on the beliefs and values of other people.

### **4.3 The Keynesian revolution and the neoliberal counterrevolution**

Another useful way of viewing Hayek’s work is by contrasting him with his intellectual rival, English economist John Maynard Keynes (1883-1946). In 1936 Keynes published the *General theory of employment, interest, and money*, which set out to challenge the entire “classical” corpus of economic thought.<sup>52</sup> As a reaction to the Great Depression of the 1930s, Keynes proposed economic policy focused on the demand side of the economy, i.e. on consumption (which was contrary to the more classical supply side approach, i.e. a focus on production). In his view, the government should

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<sup>50</sup> Boettke, “Austrian School of Economics,” in *The Concise Encyclopedia of Economics*.

<sup>51</sup> Hayek, “Economic Control and Totalitarianism,” in *The Road to Serfdom*.

<sup>52</sup> Polanyi-Levitt, “The Power of Ideas: Keynes, Hayek, and Polanyi,” p. 7: “His target was the entire corpus of English economic thought from David Ricardo to John Stuart Mill to Alfred Marshall and Arthur Pigou, which he dismissed as “classical.””

stimulate the economy via public works to combat unemployment, which would in turn increase national consumption and thereby further improve economic conditions. Although Hayek regarded Keynes as a brilliant thinker, he was one of the most prominent contemporary critics of Keynes's work. For example, in chapter 9 of *The Road to Serfdom* he warned for the anti-competitive effects of Keynesian demand management policies and the progressively increasing dependence on government expenditure.<sup>53</sup> It was Hayek's commitment to warn against various kinds of economic planning – from softer versions like the New Deal in the United States to the harder versions of fascism, Nazism and communism on the European continent – that would lead to the construction of the neoliberal paradigm, to be popularized in the 1970s and '80s. It must be noted, however, that he made a distinction between merely anti-competitive policies and the “dangerous” venture of central economic planning. The etymology of *neoliberalism* can be traced back to a Paris conference in 1938, which Hayek and Mises attended.<sup>54</sup> The term was coined as an updated version of the liberal position, which stood against collectivism and economic planning, but did acknowledge the faults of *laissez-faire* economics. After the Second World War, Keynesian economics gained a lot of traction in the 1950s and '60s, forming the political development which invited the neoliberal counterrevolution. The neoliberal project was predicated on the idea of a limited but strong government maintaining the Rule of Law and encouraging the growth of private enterprises that are steered by the forces of free market competition. Neoliberalist policies were most famously propelled by Margaret Thatcher in Great Britain and Ronald Reagan in the United States during the 1980s.

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<sup>53</sup> Hayek, “Security and Freedom,” in *The Road to Serfdom*.

<sup>54</sup> Polanyi-Levitt, “The Power of Ideas: Keynes, Hayek, and Polanyi,” p. 10: “In 1938, Mises and Hayek attended a colloquium in Paris in honor of the eminent American journalist and public intellectual Walter Lippmann. Here the term neoliberalism was coined to stake out a new liberal position on socialism and collectivism, which acknowledged that *laissez-faire* was an anachronism. Among the participants were Michael Polanyi, Raymond Aron, and Louis Rougier (Van Horn and Mirowski 2009).”



## 5. Conclusion

In the previous chapters we have established the argument of *The Road to Serfdom*, Hayek's philosophical axioms and the origins of his ideas. In this final chapter, we discuss how contemporary China relates to the practice of central planning and then draw a conclusion with respect to the research question of this thesis.

### 5.1 The case of China

The 20<sup>th</sup> century became the age in which Hayek was proven right about the totalitarian dangers of central economic planning. Throughout the post-war period, sooner or later, most countries with collectivist regimes have turned to the free market system again: most notably Germany and Italy after losing the Second World War in 1945, and Russia after the collapse of the Soviet Union in 1991. There is, however, one important example of a country that to this day remains partly committed to the practices of economic planning, namely The People's Republic of China. After a period of the first five consecutive Five-Year Plans (starting in 1953), since 1978 China has been implementing free market reforms in its Plans and opening up to foreign trade and investment. In this way, the Chinese economy has been transformed to a mixed economy over the past decades, combining important features of a market economy and a planned economy. Planning is done by a central body setting economic and (social) demographic targets and guiding principles in areas ranging from the gross domestic product (GDP), employment and research expenditure to population size, schooling and energy use.<sup>55</sup> The plan is executed by means of directing state-owned enterprises and government agencies to produce certain goods and services, while influencing private enterprises via government projects and fiscal or monetary policy.<sup>56</sup> The coexistence of state-owned and private enterprises who may compete with each other to increase economic efficiency is nevertheless a notable free market characteristic. The practice of planning symbolizes the collectivist tradition, which stands in stark contrast with the individualist tradition of Western civilization. Moreover, being under the sole leadership of the Communist Party, China is a hallmark of a state with a government that is strong and fairly effective (compared to limited government associated with the Rechtsstaat and the ineffectiveness of divided

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<sup>55</sup> Chow, "Economic Planning in China," p. 4.

<sup>56</sup> Chow, "Economic Planning in China," p. 5.

politics associated with democracy). China's free market reforms would perhaps in Hayek's view be seen as a first step towards economic freedom and therefore towards the possibility of civil and political liberty. The case of China makes clear, however, that a country with high economic growth, having shown "the fastest sustained expansion by a major economy in history,"<sup>57</sup> does not necessarily become more free as long as some structural elements of economic planning are held in place. The totalitarian power of the Chinese state has consolidated to such extent – entailing far-reaching mass surveillance of civilians, state censorship, and re-education camps detaining minorities and (political) dissidents – that civil and political liberty in the classic (negative) sense are very limited and fragile at the least, if not absent in some cases. This situation might well be what the modern and sustainable end destination of the Hayekian road to serfdom looks like.

## **5.2 The flower of liberalism**

The purpose of this thesis was to reflect on Hayek's *The Road to Serfdom* and in particular investigate why Hayek thought that central economic planning would inevitably lead to the destruction of personal and political freedom. The answer to this comes down to the argument that no complete ethical code of values exists to correctly direct economic activity from a central body. In a planning system it is thus inevitable that, sooner or later, that central body should impose its values on other people and tyrannize them in the process of enforcing the plan. Therefore it is concluded that no civil freedom can exist without economic freedom. Hayek's argument for personal freedom is driven by his belief in the philosophy of individualism and the essential role this tradition plays with respect to the progress of civilization, which he thought has been made possible by the liberty provided by the Rule of Law and impersonal free market forces. All in all, this thesis argued for the preservation of (economic) liberty and the relevance of individualism and classical liberalism today. It is of great importance that we should understand how society works to reach progress and cherish what is at the foundation of our most precious and historically unique fundamental value of liberty: the individualist tradition of Western civilization.

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<sup>57</sup> Morrison, "China's Economic Rise: History, Trends, Challenges, and Implications for the United States."

*“The attitude of the liberal toward society is like that of the gardener who tends a plant and, in order to create the conditions most favorable to its growth, must know as much as possible about its structure and the way it functions.”<sup>58</sup>*

– F.A. Hayek

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<sup>58</sup> Hayek, “The Abandoned Road,” in *The Road to Serfdom*, p. 71.

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