

AT THE ORIGINS OF NEO-LIBERALISM: THE FREE ECONOMY AND THE STRONG STATE, 1930–1947*

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ABSTRACT. *It is often suggested that the earliest theorists of neo-liberalism first entered public controversy in the 1930s and 1940s to dispel the illusion that the welfare state represented a stable middle way between capitalism and socialism. This article argues that this is an anachronistic account of the origins of neo-liberalism, since the earliest exponents of neo-liberal doctrine focused on socialist central planning rather than the welfare state as their chief adversary and even sought to accommodate certain elements of the welfare state agenda within their market liberalism. In their early work, neo-liberal theorists were suspicious of nineteenth-century liberalism and capitalism; emphasized the value commitments that they shared with progressive liberals and socialists; and endorsed significant state regulation and redistribution as essential to the maintenance of a free society. Neo-liberals of the 1930s and 1940s therefore believed that the legitimation of the market, and the individual liberty best secured by the market, had to be accomplished via an expansion of state capacity and a clear admission that earlier market liberals had been wrong to advocate laissez-faire.*

I

A familiar theme in the literature on neo-liberalism is what David Harvey has called its ‘long march’ through the institutions of post-war civil society, a trek which famously culminated in the dramatic neo-liberal moment of the 1980s, when the arduous years in the wilderness finally gave way to great political influence and the patronage of the leading politicians of the age. The main burden of this literature is that the emergence of neo-liberalism as a political force was preceded by many years of careful intellectual work by an international network

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* This article greatly benefited from presentation to the Oxford History of Political Thought seminar in November 2007; the Political Studies Association Labour Movements Group conference in June 2008; and the Cambridge Modern Economic and Social History seminar in February 2009. For invaluable comments and suggestions, I am grateful to the audiences on those occasions and to Martin Daunton, Clare Jackson, Desmond King, Melissa Lane, Gregg McClymont, Marc Stears, Zofia Stemplowska, Simon Szreter, Richard Toye, and two anonymous *Historical Journal* referees. The following people and institutions kindly granted permission to quote from private papers: Bruce Caldwell; Christopher Johnson; the Ludwig von Mises Archive at Grove City College; and the Karl Popper Library at the University of Klagenfurt.

of committed and talented sympathizers, and by a concerted effort to disseminate neo-liberal ideas through key opinion-forming institutions in the industrialized nations, notably the universities, think-tanks, business organizations, and the media.¹ In this article, I want to cast fresh light on this familiar story by examining the political thought of neo-liberalism at the very beginning of its journey through civil society. While the outline of the ‘long march’ narrative just summarized is certainly correct, I nonetheless argue that, at a more detailed level, insufficient attention has hitherto been paid to the evolution of neo-liberal ideas themselves during the course of their rise to intellectual hegemony. In particular, I contest an unhistorical assumption implicit in one common account of the rise of neo-liberal doctrine; namely, that the most influential theorists of a revival of market liberalism first entered public controversy in the 1930s and 1940s to dispel the growing illusion that the welfare state represented a stable middle way between capitalism and socialism.² Such an account anachronistically presents the early work of neo-liberal theorists as occupying precisely the same ideological space as the neo-liberalism of the 1970s. It therefore misidentifies the primary target of neo-liberal theorists in the mid-twentieth century; underestimates the degree to which neo-liberal political thought evolved and mutated over the course of the post-war period; and portrays the ideology of neo-liberalism as systematic and self-confident at a time when it was in fact incomplete and uncertain.

In making this case, I build on important research that has already begun to explore such arguments. In particular, the work of Bernhard Walpen on the Mont Pèlerin Society; Philip Mirowski and Robert Van Horn on the Chicago

¹ K. Hoover and R. Plant, *Conservative capitalism in Britain and the United States* (London, 1989), p. 27; R. Desai, ‘Second-hand dealers in ideas: think-tanks and Thatcherite hegemony’, *New Left Review*, 203 (1994), pp. 27–64; R. Cockett, *Thinking the unthinkable: think-tanks and the economic counter-revolution, 1931–1983* (London, 1995); R. M. Hartwell, *A history of the Mont Pèlerin Society* (Indianapolis, IN, 1995); A. Gamble, *Hayek* (Cambridge, 1996); D. Yergin and J. Stanislaw, *The commanding heights* (New York, NY, 2000), pp. 74–138; F. Denord, ‘Le prophète, le Pèlerin et le missionnaire: la circulation internationale du néo-libéralisme et ses acteurs’, *Actes de la Recherche en Sciences Sociales*, 145 (2002), pp. 9–20; B. Caldwell, *Hayek’s challenge: an intellectual biography of F. A. Hayek* (Chicago, IL, 2004); B. Walpen, *Die offenen Feinde und ihre Gesellschaft: Eine hegemonietheoretische Studie zur Mont Pèlerin Society* (Hamburg, 2004); D. Plehwe, B. Walpen, and G. Neunhöffer, eds., *Neo-liberal hegemony: a global critique* (London, 2005); D. Harvey, *A brief history of neo-liberalism* (Oxford, 2005), pp. 19–22, 39–63, quote at p. 40; P. Mirowski, ‘Naturalizing the market on the road to revisionism: Bruce Caldwell’s *Hayek’s challenge* and the challenge of Hayek interpretation’, *Journal of Institutional Economics*, 3 (2007), pp. 351–72; P. Mirowski, ‘Review of Harvey, *A brief history of neo-liberalism*’, *Economics and Philosophy*, 24 (2008), pp. 111–17; J. Peck, ‘Remaking *laissez-faire*’, *Progress in Human Geography*, 32 (2008), pp. 3–43; M. Foucault, *The birth of biopolitics: lectures at the Collège de France, 1978–1979* (Basingstoke, 2008); R. Turner, *Neo-liberal ideology: history, concepts and policies* (Edinburgh, 2008); P. Mirowski and D. Plehwe, eds., *The road from Mont Pèlerin: the making of the neo-liberal thought collective* (Cambridge, MA, 2009).

² The classic account in this vein is Cockett, *Thinking*, pp. 35–56, 59–62, 77, 78, 86–8. This view is also implicit in political commentary on neo-liberalism from both the left and the right: e.g. N. Barry et al., *Hayek’s ‘serfdom’ revisited* (London, 1984), pp. 5, 20–1, 89–94; N. Klein, *The shock doctrine* (London, 2007), pp. 49–57. For a brief criticism of Cockett in a similar vein to the one documented in this article see Alan Peacock’s review in *Economic Affairs*, 15 (1995), p. 52. I am grateful to Peter Sloman for drawing this reference to my attention.

School; and Jeremy Shearmur on F. A. Hayek and Karl Popper has, in various ways, started to chip away at those resolutely non-historical accounts of neo-liberal institutions and doctrines.³ As Walpen and Mirowski have both rightly identified, for example, it is highly misleading to present the eventual triumph of neo-liberalism in idealist terms, as an achievement that came about simply because of the incisive thinking and writing of great minds. Instead, it was crucial to the successful conclusion of the neo-liberals' long march that they were able to mediate their ideas through a number of interlocking institutions dedicated to developing, organizing, and popularizing their cause. The starting point for this institutional history is usually taken to be the founding of the Mont Pèlerin Society, at Hayek's initiative, in 1947, although an earlier meeting between some of the key figures in the nascent movement, at the 'Colloque Walter Lippmann' in Paris in 1938, prefigured the historic first gathering at Mont Pèlerin and has also been widely discussed.⁴

Nonetheless, it is clearly of some interest to determine why a number of intellectuals scattered across the world felt a sufficient sense of political comradeship to band together in 1947. In his address to the very first session of the Mont Pèlerin Society, Hayek was in no doubt that the founding members shared key concerns: 'I have had the good fortune in the last two years to visit several parts both of Europe and America and I have been surprised at the number of isolated men I found everywhere, working on essentially the same problems and on very similar lines.'⁵ This article fills in the intellectual backstory to Hayek's statement. It supplies a detailed map of the ideological exchanges, agreements, and tensions that subsisted among the members of this international network prior to their first full summit meeting and therefore serves as a prolegomenon to research on the institutionalization of neo-liberalism. In the process, it also questions Hayek's claim that he and his colleagues were indeed 'isolated' from one another, or that it was only since 1945 that Hayek had been struck by their common interests. Instead, it becomes apparent that, from the mid-1930s onwards, a considerable amount of time had already been invested in developing personal and intellectual connections between many

³ Walpen, *Die offenen Feinde*; Mirowski, 'Review of Harvey'; R. Van Horn and P. Mirowski, 'The rise of the Chicago School of Economics and the birth of neo-liberalism', in Mirowski and Plehwe, eds., *Road from Mont Pèlerin*; J. Shearmur, *Hayek and after* (London, 1996), pp. 3–5, 53–64; J. Shearmur, *The political thought of Karl Popper* (London, 1996), pp. 24–36, 50–7, 109–15; J. Shearmur, 'Hayek, Keynes and the state', *History of Economics Review*, 26 (1997), pp. 68–82; J. Shearmur, 'Hayek's politics', in E. Feser, ed., *The Cambridge companion to Hayek* (Cambridge, 2006), pp. 148–70.

⁴ For details of these early organizational initiatives, see Cockett, *Thinking*, pp. 54–6, 67–77, 100–21; Hartwell, *History*, especially pp. 20–99; F. Denord, 'Aux origines du néo-libéralisme en France: Louis Rougier et le Colloque Walter Lippmann de 1938', *Le Mouvement Social*, 195 (2001), pp. 20–9; Walpen, *Die offenen Feinde*, pp. 51–61, 84–93, 98–117.

⁵ F. A. Hayek, 'Address to the Mont Pèlerin conference', 1 Apr. 1947, typescript, F. A. Hayek papers, Hoover Institution Archives, Stanford University (hereafter Hayek), 71–7, pp. 2–3.

of the individuals who later assembled for their first plenary session at Mont Pèlerin.⁶

The core themes of the nascent neo-liberal political thought of this period were, unsurprisingly, a vision of the free society and a critique of the threat to freedom posed by the encroaching power of the state. Although the defence of personal liberty in the face of expanded state responsibilities has been a familiar theme in political argument since at least the late nineteenth century – we might think here of such texts as Herbert Spencer's *Man versus the state* (1884) or Hilaire Belloc's *The servile state* (1912) – the long-running debate about freedom and the state entered a distinctive new phase in the 1930s as theorists sympathetic to market liberalism grappled with the implications of such disturbing developments as Soviet central planning, the New Deal, the Popular Front government in France, and the rise of fascism. At the same time, the intellectual vitality of socialist thought and the convergence of certain strands of reformist socialism with Keynesian economics created a powerful ideological assault on the principles and practice of classical liberalism. The pendulum of expert opinion appeared to be swinging slowly, but surely, away from capitalism, a perception all but confirmed during the Second World War as nominally capitalist nations unleashed unprecedented state power over their economies and allied with the Soviet Union to wage total war on fascism.⁷

The most influential, and probably most intellectually compelling, text to be written in response to these developments was Hayek's *The road to serfdom* (1944), but this was only one of a slew of similar books and articles written in this period by a number of anxious liberal intellectuals. Whilst Hayek played a critical role in bringing together and mobilizing these allies, he was certainly not alone in taking up ideological arms in defence of liberty. One immediate source of support was the group of central European exiles resident in the English-speaking nations, such as Hayek's mentor Ludwig von Mises; the economist Fritz Machlup; the Hungarian scientist Michael Polanyi; and Karl Popper, who was recruited by the London School of Economics (LSE) from New Zealand at Hayek's urging. In this period, Hayek also enjoyed cordial relations with the German economists later known as the 'ordo-liberals'. Although ideological and personal differences subsequently emerged between Hayek and some ordo-liberals in the 1950s and 1960s, in the 1930s and 1940s figures such as Wilhelm Röpke, Alexander Rüstow, and Walter Eucken were largely of a like mind to Hayek and the other key neo-liberal theorists. In the United States, the earliest members of the Chicago School were

⁶ In this period we can also observe the earliest use of the term 'neo-liberal' itself to refer to those seeking to modernize the market liberal tradition: for examples, see Denord, 'Aux origines du néo-libéralisme', pp. 11–13, 24.

⁷ Neo-liberals such as Hayek obviously accepted that this assertion of state power was necessary during wartime in order to defeat the Nazis, but they worried that the distinction between the necessities of war and the need for a more liberal regime in peacetime would not be understood by elite or public opinion. See F. A. Hayek, *The road to serfdom*, ed. B. Caldwell (Chicago, IL, 2007 [1944]), p. 213.

also closely involved in the effort to rehabilitate market liberalism, notably Henry Simons, Frank Knight, and, more peripherally at this stage, the young Milton Friedman. They were joined by compatriots such as the Princeton economist, Frank Graham, and, more surprisingly, the sometime progressive theorist and influential political journalist, Walter Lippmann. In Britain, several prominent economists also allied themselves with Hayek, such as Lionel Robbins at the LSE; John Jewkes at Manchester; and W. H. Hutt, who had moved from the LSE to South Africa in 1928. William Rappard, the Swiss historian and diplomat, was, like Hayek, important in bringing together the various branches of this network. Finally, there were also sympathizers in France, in particular the philosopher Louis Rougier, who organized the first summit meeting of some of these characters in Paris at the ‘Colloque Walter Lippmann’, a seminar that Rougier convened specifically to discuss Walter Lippmann’s influential book, *The good society* (1937). Most of the individuals just cited were also present at the inaugural meeting of the Mont Pèlerin Society in 1947, or were to join the Society soon after, the exceptions being Simons, who died in 1946; Rougier, whose war-time dalliance with the Vichy regime in France rendered his presence in the Society unacceptable until 1956; and Lippmann, who was a founding member of the Society but never evinced any interest in attending its meetings or playing an active part in its affairs.

This over-view of early neo-liberal thinkers is not exhaustive, but it gives some sense of the broader network of figures whose overlapping ideas were influential at the intellectual origins of neo-liberalism.⁸ In the rest of this article, I argue that a close examination of these overlapping ideas in fact demonstrates that the earliest exponents of neo-liberal ideology focused primarily on socialist central planning rather than on the welfare state as their chief adversary and even sought to accommodate certain elements of the welfare state agenda within their liberalism as a means of legitimating the market.

II

The first wave of neo-liberal political thought slowly emerged into public view during the 1930s, and reached a raucous apotheosis with the highly politicized reception of *The road to serfdom* in 1944–5. The emerging movement’s leading figures were in private communication with one another throughout that time, even during the war, and usually read and commented on one another’s work. As a result of their wide-ranging private and public conversations, a distinctive set of shared political precepts began to take shape. Underpinning these precepts was an unwavering conviction that a purely defensive posture on the part of those in favour of market liberalism would hand the initiative to its enemies. Instead,

⁸ For a full list of the individuals involved in the ‘Colloque Walter Lippmann’ and the founding members of the Mont Pèlerin Society, see Walpen, *Die offenen Feinde*, pp. 60–1, 391–2; Hartwell, *History*, p. 51.

neo-liberals argued that it was necessary to articulate a new, positive vision of economic liberalism, which would offer not just a critique of harmful forms of state intervention in the economy, but also a full agenda of liberal reforms that would remake the prevailing economic disorder into the basis for a prosperous, harmonious, and free society. In particular, as both Rüstow and Simons stressed in the early 1930s, this positive agenda should be premised on forging a ‘strong state’, capable of exercising control over powerful economic interest groups, and a ‘free economy’, characterized above all by the private ownership of the means of production and the use of the price mechanism to allocate resources.⁹ Three features of this outlook drive home the distance to be travelled before this nascent ideology could mutate into the mature neo-liberalism that would win political favour in the late twentieth century: first, the early neo-liberal suspicion of nineteenth-century capitalism and liberalism; second, the emphasis of neo-liberals in the 1930s and 1940s on the value commitments that they shared with progressive liberalism and socialism; and third, the early neo-liberal endorsement of significant state regulation and redistribution as essential to the maintenance of a free society.

First, neo-liberal writers presented their ideas as improving on significant weaknesses in nineteenth-century capitalism and liberalism. Although some affection was expressed in this literature for William Gladstone and J. S. Mill,¹⁰ figures such as David Ricardo, Jeremy Bentham, and Herbert Spencer were actually subjected to considerable criticism by neo-liberals, as indeed was the whole ideology of ‘Manchester liberalism’. By ‘Manchester liberalism’ they understood a characteristic nineteenth-century belief that the market should be seen as a self-regulating mechanism and that the state’s role was to remove itself as far as possible from intervening in it or regulating it. Lippmann explicitly stated that using the ideal of *laissez-faire* to guide public policy was ‘based on so obvious an error that it seems grotesque’.¹¹ Indeed, Lippmann and his colleagues made the further point that the result of this philosophy – nineteenth-century capitalism – was morally disreputable. Jewkes, for example, claimed that ‘the socialist attacks on the social rigidities and privileges of Victorian England were sound and...were successful in paving the way for a greater measure of economic equality and the break-down of many vested interests’.¹² Popper even indicated

⁹ A. Rüstow, ‘Freie Wirtschaft – starker Staat – Die staatspolitischen Voraussetzungen des wirtschaftspolitischen Liberalismus’, *Schriften des Vereins für Sozialpolitik*, 187 (1932), pp. 62–9; H. C. Simons, *A positive program for laissez-faire: some proposals for a liberal economic policy* (Chicago, IL, 1934), pp. 1–16. See also W. Eucken, ‘Staatliche Strukturwandlungen und die Krisis des Kapitalismus’, *Weltwirtschaftliches Archiv*, 36 (1932), pp. 297–321; F. A. Hayek, ed., *Collectivist economic planning* (London, 1935); A. J. Nicholls, *Freedom with responsibility: the social market economy in Germany, 1918–1963* (Oxford, 1994), pp. 32–59. The slogan ‘the free economy and the strong state’ was of course later made famous by Andrew Gamble as a crystallization of the statecraft and ideology of Thatcherism: see his *The free economy and the strong state* (2nd edn, Basingstoke, 1994).

¹⁰ Admiration for Gladstone was expressed in e.g. Hayek, *Road*, p. 194.

¹¹ W. Lippmann, *The good society* (London, 1937), pp. 184–92, 239–40, 297–8, quote at p. 186.

¹² J. Jewkes, *Ordeal by planning* (London, 1948), p. 223.

that he fundamentally agreed with Karl Marx as an analyst of a free market economy. ‘Not much can be said against Marx’s analysis as a description of *laissez-faire* capitalism’, he wrote, since Marx lived at a time when the rhetoric of freedom was used to sanction ‘a life of desolation and misery’ for the working class. Marx’s ‘burning protest against these crimes’, Popper argued, ‘will secure him forever a place among the liberators of mankind’.¹³

Simons, Hutt, Hayek, and Robbins did not go as far in voicing full-throated criticism of the nineteenth-century legacy, but this does not mean that they should be classified as uncompromising ‘paleo-liberals’ of the same type as Mises, who was in fact the only author associated with this group to defend uncompromisingly the night watchman state.¹⁴ Instead, they insisted that nineteenth-century liberalism should not be understood ‘as a merely do-nothing policy’, but rather as a doctrine sanctioning a considerable role for the state in maintaining the legal and institutional order necessary for competitive markets.¹⁵ As Robbins argued in a letter to Lippmann about *The good society*, ‘I am entirely at one with you in rejecting *laissez-faire*’, but Robbins also suggested to Lippmann that many nineteenth-century liberals would have agreed. Robbins claimed that figures such as Jevons, Sidgwick, and Cannan were all ultimately on the same track as Lippmann.¹⁶ Likewise, although Hayek was keen to defend the broad record of nineteenth-century liberalism, he was careful in *The road to serfdom* to distance himself from the *laissez-faire* principle. ‘Probably nothing has done so much harm to the liberal cause’, Hayek wrote, ‘as the wooden insistence of some liberals on certain rough rules of thumb, above all the principle of *laissez-faire*.’ This was, he added, ‘a highly ambiguous and misleading description of the principles on which a liberal policy is based’.¹⁷ As he later elaborated in his opening paper at Mont Pèlerin, Hayek believed nineteenth-century liberals should not ‘have given the impression that the abandonment of all harmful or unnecessary state activity was the consummation of all political wisdom’ and that

¹³ K. Popper, *The open society and its enemies* (2 vols., London, 1945), II, pp. 158, 113–14; see also pp. 129–32, 166–7, 174–5, 181–2; I, pp. 97–8, 115. The definitive account of Popper’s sympathy with certain forms of socialism in this period is M. M. Hacothen, *Karl Popper: the formative years, 1902–1945* (Cambridge, 2000), especially pp. 383–520. For other examples of neo-liberal criticism of the nineteenth-century liberal preference for *laissez-faire*, see L. Rougier, *Les mystiques économiques: comment l’on passe des démocraties libérales aux états totalitaires* (Paris, 1938), pp. 34, 79–84; *Compte-rendu des séances du Colloque Walter Lippmann* (Paris, 1939), pp. 13–17, 32, 37–8, 62, 91–2; A. Rüstow, ‘Appendix’, in W. Röpke, *International economic disintegration* (London, 1942), pp. 268–74; W. Röpke, *Die Gesellschaftskrisis der Gegenwart* (Zurich, 1942), pp. 87–90, 300–3; M. Polanyi, *The logic of liberty* (London, 1951), pp. 169, 187.

¹⁴ I return to the differences between Mises and the rest of this group in section III. The phrase ‘paleo-liberal’ was coined by Rüstow: E. Megay, ‘Anti-pluralist liberalism: the German neo-liberals’, *Political Science Quarterly*, 85 (1970), pp. 424–7; Walpen, *Die offenen Feinde*, pp. 57, 323 n. 39.

¹⁵ Simons, *Positive*, p. 3.

¹⁶ Robbins to Lippmann, 8 Aug. 1937, Walter Lippmann papers, Manuscripts and Archives, Yale University Library (hereafter Lippmann), 1810. A more extended argument about the political ‘misrepresentation’ of classical economists and the industrial revolution was given by W. H. Hutt, *Economists and the public* (London, 1936), pp. 128–78.

¹⁷ Hayek, *Road*, pp. 71, 118.

the question of positive state action ‘offered no serious and important problems on which reasonable people could differ’.¹⁸

Second, the neo-liberal critique of socialism and left-liberalism was not, at this stage, primarily targeted at leftist political ideals, but rather aimed at the methods that socialists or left liberals sought to use to achieve their goals. In particular, the neo-liberal argument was not, as it would later become, that the left was necessarily wrong to pursue greater equality, social justice or economic security, but that the use of economic planning to obtain these ends would in fact vitiate any hope of achieving them and would decisively undermine individual liberty in the process. Simons opened his *Positive program for laissez-faire* with the observation that ‘there is in America no important disagreement as to the proper objectives of economic policy – larger real income, greater regularity of production and employment, reduction of inequality, preservation of democratic institutions. The real issues have to do merely with means, not with ends.’¹⁹ Even among neo-liberals based in Europe, there was a widespread view that liberals and socialists shared a number of value commitments despite differing over their policy implications. It was therefore the misguided application of these values that the neo-liberals sought to correct. This perspective comes out very clearly in the writings of, for example, Alexander Rüstow, Michael Polanyi, Popper, and W. H. Hutt. Popper wrote to Hayek that a crucial objective of any liberal revival should be ‘getting over the fatal split in the humanitarian camp’ by ‘uniting the vast majority of liberals and socialists (as it were, under the flags of Mill and Lippmann)’.²⁰ Meanwhile, Hutt argued that liberty, security, and equality were entirely compatible values; in his view they only became incompatible if equality was sought through totalitarian methods. He even claimed that his favoured policy proposals ‘can bring about the achievement of every ideal of which the democratic socialists have dreamed’.²¹

Hayek’s position was more ambiguous. He famously wrote *The road to serfdom* with the aim of persuading progressive liberals and socialists of the error of their ways, and much of the book was indeed devoted to establishing that significantly greater unfreedom, inequality, and insecurity would emerge in a planned economy than would exist in a market order.²² As is well known, Popper suggested to Hayek in 1947 that the Mont Pèlerin Society should be open to liberal socialists as

¹⁸ Hayek, ‘Free enterprise and competitive order’, typescript, 1947, Hayek 81–3, p. 5; reprinted in F. A. Hayek, *Individualism and economic order* (London, 1948), p. 109.

¹⁹ Simons, *Positive*, p. 1.

²⁰ Popper to Hayek, 15 Mar. 1944, Karl Popper papers, microfilm, LSE Library (hereafter Popper), 305.13.

²¹ Hutt, *Economists and the public*, pp. 313–47; his *Plan for reconstruction* (London, 1943), pp. 137–45, 310–11, quote at p. 310; Rüstow, ‘Appendix’, pp. 281–3; Polanyi, *Logic*, p. 144.

²² E.g. Hayek, *Road*, pp. 137–8, 149–56. Some contemporary critics of Hayek also took him to be attacking socialist means rather than socialist ends: H. Dickinson, ‘Review of *Freedom and the economic system*’, *Economica*, 7 (1940), p. 435; A. C. Pigou, ‘Review of *The road to serfdom*’, *Economic Journal*, 54 (1944), pp. 217–18; E. Durbin, ‘Professor Hayek on economic planning and political liberty’, *Economic Journal*, 55 (1945), pp. 357–9.

well as to neo-liberals. Less widely noted is that, in this letter, Popper made it clear that he and Hayek had already discussed this strategic issue informally. Popper observed: ‘My own position, as you will remember, was always to try for a reconciliation of liberals and socialists; with this tendency you were in sympathy.’²³ One further piece of evidence suggests that Hayek had at least entertained this possibility. In a lecture given at Stanford in 1946, Hayek floated his long-standing interest in organizing an international network aimed at reviving liberal values. He gave a surprisingly inclusive account of the potential membership of such a network, describing an emerging liberal movement ‘which stretches from what one might call certain liberal socialist groups at the one extreme to certain liberal catholic groups on the other’, bound together by a belief ‘that personal liberty is the highest political good, more important than security’.²⁴ Of course, the invitation list for the first meeting of the Mont Pèlerin Society was more narrowly drawn in the end, and even Hayek’s inclusive remarks at Stanford cut both ways, since they assumed a strict trade-off between freedom and economic security. Nonetheless, at this time Hayek, as he made clear in his opening paper at Mont Pèlerin, certainly claimed that certain efforts to promote greater economic security and equality were compatible with a free society.²⁵

Hayek’s arguments in this vein did not sit easily with other points he made elsewhere, which gestured towards his later comprehensive critique of patterned principles of justice. For example, he signalled that he was worried about broad principles such as ‘equality’ and ‘distributive justice’ which sought to impose detailed rankings of social value on the distribution of income and wealth; like ‘the common good’, Hayek thought that, under a regime of planning, these objectives would simply serve as masks for the sectarian agenda of dominant interest groups.²⁶ Nonetheless, as discussed later, in the same work Hayek did endorse the state enforcement of some sort of distributive pattern. In this respect, as in many others, *The road to serfdom* was a transitional work, in which Hayek began to feel his way towards his mature intellectual position but had not, as yet, fully developed or integrated all of its elements.

Third, neo-liberal authors were keen to emphasize that their philosophy was not reactionary and negative, but on the contrary embraced a weighty agenda of social and economic reform, a ‘positive program’, in Simon’s phrase. Their core claim was that they were not opposed to planning *tout court*, but to planning that involved the central direction of all economic resources according to a conscious

²³ Popper to Hayek, 11 Jan. 1947, Popper 305.13. Popper also argued Hayek was not a ‘reactionary’ in correspondence with Rudolf Carnap: ‘[Hayek] is certainly not a protagonist of unrestricted capitalism. On the contrary, he insists on the need of a system of “Social Security”, on anti-cycle policy, etc.’ Popper to Carnap, 25 Apr. 1946, reprinted in K. Popper, *After the open society: selected social and political writings*, ed. J. Shearmur and P. Norris Turner (London, 2008), p. 100.

²⁴ Hayek, ‘Prospects for freedom’, lecture at Stanford University, 1946, typescript, Hayek 107–7, p. 10.

²⁵ Hayek, ‘Free enterprise and competitive order’, pp. 4–5 (p. 109 in published version).

²⁶ Hayek, *Road*, pp. 100–11, 139–42.

blueprint. Instead, they advocated the design of an economic system that would enable individuals to formulate their own individual life-plans on a rational basis.²⁷ Such a system would require a strong state to enforce the rule of law and leave the resolution of most economic decisions to the free play of the price mechanism. The creation and maintenance of this putative ‘competitive order’ was, however, also thought to require certain non-market institutions and rules to ensure it functioned effectively, and it was acknowledged that its popular legitimacy would depend on certain forms of non-market social provision.

Rougier, Röpke, and Hayek all illustrated these arguments with the same image, borrowed from Lippmann’s *The good society*. The difference between their liberal philosophy and central planning, they argued, was like that between, on the one hand, constructing rules of the road to bind all drivers to the same general regulations, as in the Highway Code, and, on the other hand, ordering drivers where to drive. Alternatively, it was like the difference between providing signposts and dictating routes to drivers.²⁸ Rougier played with the image slightly. He posed a three-fold contrast, between a socialist state, ‘true’ liberalism, and ‘Manchester liberalism’. The first two were as Lippmann, Röpke, and Hayek had indicated, while ‘Manchester liberalism’, Rougier argued, was like a regime that allowed cars to drive ‘as they please without a highway code’, which resulted in ‘the law of the jungle’.²⁹ The gravest infringement of liberty, these images suggested, was granting the state the power to coerce directly the will of particular individuals, as opposed to limiting the state to the design of general rules that would apply equally to all.

A further implication was that certain kinds of state activity, certain kinds of ‘intervention’ even, could be perfectly compatible with individual liberty, provided that they did not undermine the free working of the price mechanism. As Rougier had suggested, for many neo-liberals of this period the aim was to chart, in the words of Röpke and Rüstow, a ‘third way’ between Manchester liberalism and collectivism. This point was made most explicitly by Röpke and Rüstow themselves, who both distinguished between intervention that was ‘incompatible’ with the market and intervention that was ‘compatible’. The core difference between these two seems to have turned on whether a particular intervention directly prohibited certain forms of market activity, and consequently led to greater and greater pressure on the state to undertake yet further intervention in the price mechanism or whether, on the contrary, the intervention simply altered the framework within which buyers and sellers made commercial decisions. This was, they claimed, the difference between, for example, instituting exchange

²⁷ W. Röpke, *Die Lehre von der Wirtschaft* (Vienna, 1937), pp. 185–7; L. Robbins, *Economic planning and international order* (London, 1937), pp. 4–7; Hayek, *Road*, p. 85.

²⁸ Lippmann, *Good society*, p. 283; Röpke, *Gesellschaftskrisis*, pp. 299–300; Hayek, *Road*, pp. 113–14. Lippmann also used the analogy of a whist club that, rather than restricting itself to stipulating a binding set of rules of the game for everyone, instructs players to play certain cards: *Good society*, p. 317. Keynes also used a similar rule of the road metaphor in his *How to pay for the war* (London, 1940), p. 12.

²⁹ Rougier, *Mystiques*, p. 88. He also made the same point in *Colloque Walter Lippmann*, p. 16.

controls and deciding to devalue a currency. Rüstow and Röpke also referred to ‘compatible’ intervention as ‘liberal interventionism’. Similar vocabulary was used by Popper to characterize his favoured model of ‘democratic interventionism’, to be pursued through ‘piece-meal social engineering’, as distinct from the ‘utopian engineering’ advocated by the enemies of the free society.³⁰

In correspondence with Röpke, Hayek indicated that he was unenthusiastic about the terminology of ‘compatible’ or ‘incompatible’ intervention, but broadly the same idea is conveyed in *The road to serfdom*: a distinction between forms of state activity that supplement market competition, or help to make it work more effectively, and state action that would subvert the price mechanism altogether.³¹ As Hayek elaborated when lecturing on his book in the United States in 1945, he was actually against ‘the idea that all government action or interference with business is bad’, and opposed ‘the very dangerous tendency of using the term “socialism” for almost any kind of state activity which you think is silly or which you do not like’. This, Hayek argued, was ‘crying wolf!’. Instead, liberals required ‘a set of principles which enables us to distinguish between what form of government activity is good, is necessary, and where government intervention in economic affairs is of a dangerous nature’.³² Indeed, during the course of the lengthy correspondence between Popper and Hayek about the manuscript of *The open society and its enemies*, Hayek even wrote to Popper: ‘In the sense in which you use and carefully explain these terms, I have no objection against “interventionism”’.³³

III

The state activities identified by neo-liberals in the 1930s and 1940s as infringing on liberty therefore differed from their subsequent targets: they objected mainly to economic planning, understood in a strong sense. As has been explored elsewhere, a very diverse range of economic projects were grouped together as ‘planning’ in this period, ranging from capitalist-sponsored efforts to ‘rationalize’ industries to market socialism to Soviet-style Gosplanning, with Keynes-inspired

³⁰ Rüstow, ‘Freie Wirtschaft – starker Staat’; his ‘Appendix’, pp. 274–83; W. Röpke, *German commercial policy* (London, 1934), pp. 50–1; Röpke, *Lehre*, pp. 187–93; Röpke, *Gesellschaftskrisis*, pp. 258–64; Popper, *Open society*, I, pp. 138–48, II, pp. 181–2, 318 n. 9. The ‘third way’ vocabulary was also used by Walter Eucken to characterize the implications of Hayek’s *Road to serfdom*: Eucken to Hayek, 12 Mar. 1946, Hayek 18–40, p. 3.

³¹ Röpke to Hayek, 8 July 1942, Hayek 79–1; Hayek, *Road*, e.g. pp. 85–90. See also e.g. Robbins, *Economic planning*, pp. 225–9; Rougier, *Mystiques*, pp. 84–8; M. Polanyi, *The contempt of freedom: the Russian experiment and after* (London, 1940), pp. 35–40, 59–60. In his introduction to the 1976 edition of *The road to serfdom*, Hayek noted that when writing the book ‘I had not wholly freed myself from all the current interventionist superstitions, and in consequence still made various concessions which I now think unwarranted.’ Hayek, ‘Preface to the 1976 edition’, reprinted in *Road*, p. 55.

³² F. A. Hayek, ‘Address to the Economic Club of Detroit’, 23 Apr. 1945, typescript, Hayek 106–8, p. 6.

³³ Hayek to Popper, 12 Nov. 1943, Popper 541.12. Although Hayek also indicated in the same letter that he would not personally choose to employ the term to describe his own position.

fiscal ‘planning’ often thrown in for good measure.³⁴ At this stage, neo-liberal authors focused their energies on opposing the socialist and fascist strands of this discourse. At the beginning of *The road to serfdom*, Hayek defined planning as ‘a central direction of all economic activity according to a single plan, laying down how the resources of society should be “consciously directed” to serve particular ends in a definite way’.³⁵ This was a definition that clearly had the Soviet or Nazi model of planning in mind and implicitly also included more moderate forms of market socialism, on the grounds that they prescribed an unstable ‘third way’ that would in due course skid down the slippery slope towards totalitarian control over the economy. Neo-liberals had initially objected, in the early 1930s, to the impossibility of rational economic calculation in such a centrally planned economy; the later 1930s and 1940s saw this replaced as the dominant line of neo-liberal argument by an emphasis on the destructive consequences of central planning for individual liberty.³⁶ Crucially, however, in both phases of this debate the chief enemy of the neo-liberals was not the nascent welfare state or even Keynesian economics.

Among the authors conventionally bracketed together as the founders of neo-liberalism, there was, as might be expected, a spectrum of positions on these issues, rather than a uniform line. Mises was clearly the most uncompromising member of this group who, even in this period, argued for positions that were not very different from the neo-liberalism of the 1970s. According to a famous anecdote, recounted by Milton Friedman, during one early meeting of the Mont Pèlerin Society, Mises lost his temper with the other attendees and stormed out shouting ‘You’re all a bunch of socialists!’³⁷ This anecdote resonates with Mises’s initial response to Hayek’s proposal to form the Society. Mises replied to Hayek with a memo that demanded that the new group commit itself to an unadulterated philosophy of *laissez-faire* and claimed that the weak point of Hayek’s proposal was the intention to include in the Society individuals in favour of certain forms of state intervention, such as the sometime Chicago economist Harry Gideonse and Röpke.³⁸ A further flavour of the Mises *Weltanschauung* can be gleaned from another of his letters to Hayek: ‘Do you still consider the *Economist* an excellent periodical? I think it is rather a twin brother of the *New Statesman and Nation*.’³⁹ The ordo-liberals were more or less open in their disagreements with

³⁴ D. Ritschel, *The politics of planning* (Oxford, 1997); R. Toye, *The Labour Party and the planned economy, 1931–1951* (Woodbridge, 2003); J. Tomlinson, ‘Planning: debate and policy in the 1940s’, *Twentieth Century British History*, 3 (1992), pp. 154–74; P. D. Reagan, *Designing a new America: the origins of New Deal planning, 1890–1943* (Amherst, MA, 1999).

³⁵ Hayek, *Road*, p. 85. For similar definitions, see Robbins, *Economic planning*, p. 7; Polanyi, *Contempt*, pp. 27–40; Röpke, *Gesellschaftskrisis*, pp. 38–40; Jewkes, *Ordeal*, pp. x–xi, 1–3. On this point, see also Shearmur, ‘Hayek, Keynes and the state’, pp. 71–3.

³⁶ For the earlier phase of the neo-liberal critique, see Hayek, ed., *Collectivist economic planning*.

³⁷ Cockett, *Thinking*, p. 114; M. Friedman and R. Friedman, *Two lucky people: memoirs* (Chicago, IL, 1998), p. 161.

³⁸ Mises to Hayek, 31 Dec. 1946; L. von Mises, ‘Observations on Professor Hayek’s plan’, 31 Dec. 1946, typescript, both Hayek 38–24.

³⁹ Mises to Hayek, 18 July 1943, Hayek 38–24.

Mises; it was Rüstow who first dubbed him a 'paleo-liberal'. Both the published record of the Colloque Walter Lippmann and the unpublished rough notes of the first meeting of the Mont Pèlerin Society suggest that Mises invariably occupied the rightmost flank of the discussion.⁴⁰ However, it is also clear from private correspondence that even Mises's Austrian friends and allies had reservations about his politics. Although his colleagues remained loyal in public, much hand-wringing went on in private about Mises's dogmatic character and his lack of political sophistication; Machlup was particularly vocal on this score in his letters to Hayek.⁴¹ Hayek was more discrete, but even he expressed doubts, noting in a letter to the economist, Allan Fisher, that 'the somewhat extreme and frequently naïve views' at times expounded by the free market publicist, Henry Hazlitt, 'seem to derive from our old friend Mises, with whom Hazlitt is on very intimate terms, and from whom he derives most of his economics'.⁴²

Mises's colleagues were therefore open to a different policy agenda. As Graham remarked in response to a typical remark by Mises at the first Mont Pèlerin Society conference: 'If we carry out the suggestions of Prof. Mises we shall be in the jungle. We are here met to find the middle road between the jungle and the jail.'⁴³ Walter Lippmann's book is a good example in this respect: it was a text considered of sufficient interest to assemble the emerging movement's leading figures in Paris in 1938, but in fact proposed a good society that would be quite unacceptable to later neo-liberals. Although Lippmann had by then emerged as a critic of the New Deal, his objections were primarily procedural rather than substantive: he abhorred Roosevelt's attempt at court-packing in February 1937 and the lack of congressional scrutiny accorded to Roosevelt's tax proposals in 1935. When Lippmann outlined his positive proposals for public policy in *The good society* they included social insurance; smaller corporations; higher public investment in education and health; the gradual equalization of wealth through 'drastic inheritance and steeply graduated income taxes'; and the use of public works programmes and public investment to reduce unemployment, the latter point explicitly drawn from the arguments of Keynes's *General theory*. The book's

⁴⁰ *Colloque Walter Lippmann*, pp. 41–2, 60–1, 74, 88–90; notes from session on 'Free enterprise and competitive order', 1 Apr. 1947, first meeting of Mont Pèlerin Society, Hayek 81–3.

⁴¹ See e.g. Machlup to Hayek, 14 Mar. 1941, 21 Oct. 1943, 2 Aug. 1944, 24 Aug. 1944, all Hayek 36–17. For an example of public criticism of Mises from within neo-liberal ranks, see H. Simons, 'Review of von Mises, *Omnipotent government*', *Annals of the American Academy of Political and Social Science*, 236 (1944), pp. 192–3.

⁴² Hayek to Fisher, 18 Nov. 1948, Hayek 73–32. In correspondence with Machlup, Hayek defended Mises but also acknowledged his shortcomings. In one letter, Hayek noted that although Mises's work had 'very brilliant patches', he 'has not the gift to persuade', Hayek to Machlup, 30 July 1944; see too Hayek to Machlup, 2 Jan. 1941, both in Fritz Machlup papers, Hoover Institution Archives, Stanford University (hereafter Machlup), 43–15. For similar thoughts about the complexities of the Hayek–Mises relationship, with a focus on the methodological differences between them, see Caldwell, *Hayek's challenge*, pp. 143–9, 220–3.

⁴³ F. Graham, in notes from session on 'Free enterprise and competitive order', evening session, 1 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3, p. 5.

acknowledgements not only expressed Lippmann's indebtedness to Mises and Hayek, 'whose critique of planned economy has brought a new understanding of the whole problem of collectivism', but also thanked 'Mr John Maynard Keynes, who has done so much to demonstrate to the free peoples that the modern economy can be regulated without dictatorship'.⁴⁴ Lippmann probably occupied the left-most flank of the neo-liberal debates, but he was not alone in advocating these policies. Three major policy themes in the neo-liberal literature of the 1930s and 1940s exemplified a willingness to countenance state-sponsored regulation and even redistribution: first, support for state intervention to break up large corporations; second, support for a state-sponsored social minimum and equality of opportunity; and third, a surprisingly complex attitude towards Keynes and counter-cyclical government intervention in the economy.

The first of these themes focused on the danger posed to both individual freedom and economic efficiency by large corporations and concentrations of property. Many neo-liberal authors argued that the power exercised by vast business organizations over individual workers and consumers, and the dependency bred by such power, was as destructive to the personal independence that they prized as an over-mighty state. In particular, the work of Henry Simons and the early writings of the ordo-liberals established a clear, unequivocal hostility to corporate power and stressed that state partiality to its sectional interests would only corrupt and weaken the state. As Simons put it, '*the great enemy of democracy is monopoly, in all its forms*: gigantic corporations, trade associations and other agencies for price control, trade unions – or, in general, organization and concentration of power within functional classes'.⁴⁵

One widely discussed analysis of the apparent prevalence of monopolistic companies in mid-twentieth-century capitalism, favoured in particular by Mises, was that the main culprits of this deformity of market capitalism were state intervention and protectionism. Mises therefore frequently argued that the only remedy was to return to free trade and uninhibited market forces. While other neo-liberal writers were in some respects sympathetic to this agenda, they modified it by insisting that certain forms of state activity would also be necessary to contain the great power exercised by large corporations. The classic statement of this case, very influential in neo-liberal circles at this time, was made by Simons, who included the 'elimination of private monopoly in all its forms' as the first proposal in his agenda for positive liberal reform. Simons argued that this would require serious changes to corporate law, including a legal limit on the total amount of property that could be owned by one corporation; the abolition of holding companies; prohibitions on inter-locking directorships; and a crackdown

⁴⁴ Lippmann, *Good society*, pp. xli–xlii, 212–32, quotes at pp. xli–xlii, 227. Lippmann knew Keynes fairly well: see the warm correspondence between them in the Lippmann papers, folder 1217; and R. Steel, *Walter Lippmann and the American century* (Boston, MA, 1980), pp. 304–9.

⁴⁵ Simons, *Positive*, p. 4, emphasis in original.

on the use of corporate earnings to evade income tax.⁴⁶ These proposals, which in effect amounted to a state-sponsored programme to break up large companies and concentrations of property, were later enthusiastically taken up by Lippmann, Graham, Hutt, and Röpke, whilst Hayek also seems to have been sympathetic in the 1930s and possibly 1940s.⁴⁷ Simons, Röpke, and Graham were willing to go even further. All three recommended the socialization of monopolies should free competition prove unworkable in particular industries. In particular, they favoured public ownership of 'natural' monopolies such as utilities and the railways; this was preferable, in their view, to strict government regulation of the private owners of such industries.⁴⁸ Hutt and Röpke also favoured selective public ownership of specific companies in order to provide competition to the private sector.⁴⁹ Hayek disagreed with these proposals, and although Graham raised the socialization of utilities at the Mont Pèlerin Society's first meeting, the surviving notes of the discussion suggest that it sparked controversy among the founding members rather than widespread assent.⁵⁰

There was nevertheless agreement in these circles that the creation of a free and competitive economic order would require significant state regulation of private corporations and measures designed to ensure a wider diffusion of private property. The most ambitious version of this social vision was articulated by Rüstow and Röpke. Their 'ordo-liberalism' envisaged the creation of a decentralized economy composed of smaller population centres and enterprises and characterized by a more equal spread of individual property holdings. In certain respects, they regarded an agrarian, peasant economy as embodying social virtues absent from what Röpke called the 'proletarianized society' of contemporary capitalism, which he saw as scarred by insecurity, dependence, and arbitrariness. It was not capitalism, wrote Röpke, but 'big enterprise which goes far to destroy personal independence, spontaneity of decisions, variety of action, and individual

⁴⁶ *Ibid.*, pp. 17, 19–21. For helpful discussion of Simons in this context, see Van Horn and Mirowski, 'Rise of the Chicago School', pp. 142–3; J. B. De Long, 'In defence of Henry Simons' standing as a classical liberal', *Cato Journal*, 9 (1990), pp. 601–18.

⁴⁷ Lippmann, *Good society*, pp. 216–18, 222–4, 277–81; F. Graham, *Social goals and economic institutions* (Princeton, NJ, 1942), pp. 203–22; Röpke, *Gesellschaftskrisis*, pp. 366–74, 251; Hutt, *Plan*, pp. 287–92; Hayek to Lippmann, 11 Aug. 1937, Lippmann 1011; Hayek to Machlup, 8 Aug. 1942, Machlup 43–15; Hayek, 'Address', pp. 12–13; Hayek, 'Free enterprise and competitive order', pp. 16–18 (p. 116 in published version); R. Van Horn, 'Reinventing monopoly and the role of corporations: the roots of Chicago Law and Economics', in Mirowski and Plehwe, eds., *Road from Mont Pèlerin*, pp. 209–13. Lippmann and Hutt did not explicitly refer to Simons as the source of their ideas on the reform of corporate law.

⁴⁸ Simons, *Positive*, pp. 11–12, 18, 22–3; Graham, *Social goals*, pp. 223–4; Röpke, *Gesellschaftskrisis*, pp. 306–7.

⁴⁹ W. H. Hutt, 'Economic institutions and the new socialism', *Economica*, 7 (1940), p. 431; Hutt, *Plan*, pp. 232–47; Röpke, *Gesellschaftskrisis*, pp. 306–7. Lippmann also favoured a mixture of public and private ownership: *Good society*, pp. 305–7.

⁵⁰ Van Horn and Mirowski, 'Rise of the Chicago School', p. 142; Hayek, *Road*, pp. 206–7; notes from session on 'Free enterprise and competitive order', 1 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3.

craftsmanship'.⁵¹ Rüstow and Röpke regarded the disappearance of the communal spirit and hardy independence purportedly enjoyed by the peasantry as a grave social loss and therefore argued that the life and work of the industrial worker should be rendered as similar as possible to that of a traditional artisan or peasant. To achieve this, they recommended a programme of 'deproletarianization' that included the use of significant regional planning powers to break up big cities and corporations alike; the encouragement of peasant agriculture, artisan production, and small traders; state assistance for the research and development and capital requirements of small businesses; and measures to enable workers to own their homes and a share of capital.⁵²

There was, however, one further implication of the neo-liberal stance against corporate power. Simon's passionate injunctions against monopoly, quoted earlier, castigated not only 'gigantic corporations', but also trade unions. This remark was broadly reflective of the early neo-liberal outlook, since almost all of these authors regarded trade unions as essentially identical to large corporations in their exercise of coercion, their creation of dependency, and their obstruction of the free working of the price mechanism. Unions, too, were therefore seen as excessively powerful organizations that ought to be subjected to stronger legal regulation and broken down into smaller units. In this context, the work of Hutt and Simons proved particularly influential. Hutt's *The theory of collective bargaining* (1930) and Simon's article 'Some reflections on syndicalism' (1944) both analysed trade unionism as simply another attempt by owners of a particular good to monopolize its supply. The consequence of unionization, they argued, was that the privileged insiders in trade unions reaped monopoly gains from their wage-fixing, thus advantaging themselves relative to the really disadvantaged workers, namely those working in industries that were not as easily unionized. Furthermore, this union monopoly raised prices for consumers and allowed unions to take advantage of their special state protections to exercise coercion and legalized violence through closed-shop agreements and strikes. Possible remedies included major changes to industrial relations law to reshape the trade union movement by breaking unions into firm-specific associations, or even the legal prohibition of strike action, although many prominent neo-liberals, including Simons, felt that major initiatives in this area were simply not practical politics because of the broad public support enjoyed by organized labour.⁵³ This hostility to trade

⁵¹ W. Röpke, 'Socialism, planning and the business cycle', *Journal of Political Economy*, 44 (1936), p. 323.

⁵² Röpke, *Gesellschaftskrisis*, pp. 318–57; W. Röpke, 'The proletarianized society', Parts I and II, *Time and Tide*, 1 and 8 Oct. 1949, pp. 973–4, 998–9; Rüstow, 'Appendix', pp. 279–83; Rüstow, in *Colloque Walter Lippmann*, pp. 77–83.

⁵³ W. H. Hutt, *The theory of collective bargaining* (London, 1930); his *Plan*, pp. 83–4, 273; Simons, *Positive*, pp. 9–10, 21–2; H. Simons, 'Some reflections on syndicalism', *Journal of Political Economy*, 52 (1944), pp. 1–25; Graham, *Social goals*, pp. 178–9; Robbins to Lippmann, 8 Aug. 1937, Lippmann 1810; Simons to Lippmann, 5 Oct. 1937, Lippmann 1949; Hayek, 'Free enterprise and competitive order', pp. 19–20 (p. 117 in published version); notes from session on 'Wages and wage policy', 8 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3.

unionism should, in any case, be contextualized within the broader neo-liberal case against monopolistic producer interests and the corruption of the state by pressure groups, and their disposition in favour of the interests of the individual citizen as a consumer. As Hayek put it, ‘the impetus of the movement towards totalitarianism comes mainly from the two great vested interests: organized capital and organized labour’.⁵⁴ The crucial point is that, in this period, ‘organized capital’ and ‘organized labour’ were given equal billing in the neo-liberal case for a free society. The moral equivalence between the two was, of course, not to last. In due course, ‘organized labour’ was to emerge as the principal architect of the encroaching totalitarianism of the post-war boom and as the chief target of the strong state recommended by neo-liberal theory.

As Milton Friedman observed at the first meeting of the Mont Pèlerin Society, however, it seemed to these authors that it would only be legitimate for the state to take action against the unions if the underlying problem of the low incomes and economic insecurity of the working class had first been solved.⁵⁵ The second theme to notice in early neo-liberal policy discussions is therefore a broad acceptance of the need for a state-sponsored minimum income, and of a legitimate role for fiscal policy in narrowing inequalities of opportunity. The early neo-liberals were not advocates of a completely unpatterned distribution of income and wealth, nor of constructing a market economy without a safety net. As discussed earlier, these authors did not examine in any depth, or frontally assault, the normative values recommended by the left in this period. Some undoubtedly harboured anxieties about complex patterned principles of justice that sought to compress and rearrange the relative ordering of incomes and wealth according to abstract moral criteria such as ‘equality’ or ‘social justice’. Notwithstanding this worry, however, almost all of the neo-liberals argued that a rough distributive pattern should be imposed by the state in the form of a floor constraint on income levels and the redistribution of very large concentrations of wealth; the corollary was that these neo-liberal pioneers did not believe that a properly functioning free market would itself provide every member of the community with an acceptable standard of living.

In *The road to serfdom*, Hayek explicitly conceded that there was ‘a strong case for reducing...inequality of opportunity’; indicated that legal regulations governing maximum working hours fell within his definition of the rule of law; and argued that it was desirable to guarantee a minimum level of food, shelter, and clothing to every citizen, partly because he accepted there was a sense in which progressives were correct to regard economic security ‘as an indispensable condition of real liberty’. Hayek noted that the ‘independence of mind or strength of character’ he valued ‘is rarely found among those who cannot be confident that they will make their way by their own effort’. For this reason, it was necessary for

⁵⁴ Hayek, *Road*, p. 204.

⁵⁵ M. Friedman, in notes from session on ‘Taxation, poverty and income distribution’, 8 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3, p. 1.

collective provision outside the market to establish a national minimum and to insure against sickness and accidents.⁵⁶ In this respect, Hayek's views were not radically distinct from left-wingers who also emphasized the extent to which fear and insecurity could undermine the liberty to act of disadvantaged individuals. These sentiments were amplified by Hayek's colleagues. Simons, for example, favoured increasing the progressivity of the income tax system to boost the incomes of the lowest paid and to expand social services.⁵⁷ Graham was more inclined towards proportional taxation, but also endorsed the capping or progressive taxation of very high incomes; the regulation of working hours; and a minimum wage law.⁵⁸ Popper argued for labour market regulation, social insurance, and pensions to ensure that a richer and more substantial liberty could be enjoyed by all citizens.⁵⁹ Hutt proposed probably the most detailed neo-liberal scheme along these lines in his *Plan for reconstruction* (1943), written as a post-Beveridge contribution to the British debate over post-war reconstruction. Among other proposals, Hutt envisaged workers signing up to a 'labour security bill' that guaranteed a minimum income subsidised by the state, to be uprated in line with the cost of living; the regulation of total working hours; and a system of contributory pensions and health insurance, all granted in exchange for the dissolution of the traditional rights given to trade unions to bargain collectively for wages. These measures were to be funded by a proportional levy on all incomes.⁶⁰ It was also in this period that Milton Friedman began to develop his plans for a negative income tax, a proposal that sought to replace existing welfare expenditure with a system of tax credits that ensured a minimum income for all, and which subsequently attracted the attention of policy-makers in the 1970s. Friedman presented one of the earliest versions of his scheme to the first meeting of the Mont Pèlerin Society.⁶¹ As this summary indicates, there was no clear neo-liberal line on the optimal model of income taxation. Some authors were in favour of progressive taxation, others proportional. Hayek, for example, was gradually moving towards a critique of progressive taxation, but had not yet fully developed

⁵⁶ Hayek, *Road*, pp. 118, 134, 147–9, 156, 215. In the course of a radio debate in the US on *The road to serfdom* (on 22 Apr. 1945), Hayek indicated that limits on maximum working hours and social insurance schemes were, from his point of view, legitimate functions for the state: see the transcript reprinted in S. Kresge and L. Wenar, eds., *Hayek on Hayek* (London, 1994), pp. 112–14. See also Shearmur, 'Hayek, Keynes and the state', pp. 71–2.

⁵⁷ Simons, *Positive*, pp. 26–30; Simons, 'Reflections', p. 19. Röpke also endorsed the use of redistributive fiscal policy: *Gesellschaftskrisis*, pp. 305–6.

⁵⁸ Graham, *Social goals*, pp. 177–81, 231–40; F. D. Graham, 'Keynes vs. Hayek on a commodity reserve currency', *Economic Journal*, 54 (1944), p. 428.

⁵⁹ Popper, *Open society*, II, pp. 116–18, 122–3, 129–30, 169–70.

⁶⁰ Hutt, *Plan*, pp. 5–19, 60–2, 165–85. Hayek commended Hutt's 'very interesting suggestions' and said that his plan 'will repay careful study': *Road*, p. 150 n. 5.

⁶¹ M. Friedman, in notes from session on 'Taxation, poverty and income distribution', 8 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3, pp. 1–3 and subsequent discussion. Friedman later made this proposal famous in his *Capitalism and freedom* (Chicago, IL, 2002 [1962]), pp. 190–4.

his views on this question.⁶² There was, however, general agreement among these authors that capital taxation, especially inheritance tax, represented a fair and legitimate tool for promoting equal opportunity.⁶³

We should be careful not to over-state the enthusiasm of these authors for what subsequently became known as ‘the welfare state’. They were wary of compulsory insurance schemes of the sort advocated by Beveridge, and even in this period there was concern about the potential impact of ‘welfare dependency’ if unemployment benefit was granted on too generous terms. The greatest hostility to the welfare state in this vein actually came from the ordo-liberals, later to be lauded as the ideological inspiration for the German model of welfare capitalism. Röpke, in particular, was scathing about Beveridge’s proposals, regarding them as simply compounding the dependency and proletarianization that he abhorred; the only true method of ‘deproletarianization’, he argued, was to diffuse property ownership more widely, not ‘still more social insurance, a still larger social bureaucracy, still more of pushing incomes about hither and thither, yet more labels and more stamps, yet further concentration of power, national income and responsibility in the hand of the state which is seeking to encompass, regulate, concentrate and control everything’.⁶⁴ Yet even Röpke agreed with some forms of social insurance and accepted that other welfare measures would be necessary as palliatives for the actually existing proletarians.⁶⁵ His hostility to grander proposals was not motivated by disagreement with their underlying aims. He simply believed that his model of ‘deproletarianization’, which focused on diffusing private property ownership more widely, represented a bolder and more far-reaching challenge to the ills of mass industrialized society. Neo-liberalism, although by no means egalitarian or in agreement in every particular, was in this period part of the growing consensus that the state should regulate and redistribute to provide basic minimum standards and equal opportunity for all its citizens.

Third, the opposition to Keynes was not as clear or as vociferous as might be expected in this circle. Indeed, Keynes was the cause of division and uncertainty within neo-liberal ranks. As already mentioned, Lippmann was a warm supporter of the use of counter-cyclical government intervention for Keynesian reasons. Polanyi and Popper also advocated such policies; Popper even argued that the pioneering use of counter-cyclical policies in the social democratic Sweden of the 1930s showed the way forward for other nations.⁶⁶ After the war, Jewkes and Robbins, fresh from their war work in the Economic Section of the British

⁶² Hayek, ‘Free enterprise and competitive order’, pp. 21–2 (p. 118 in printed version); F. A. Hayek, ‘The case against progressive income taxes’, *The Freeman*, 28 Dec. 1953, pp. 229–32. Hayek did not discuss taxation in any detail in *Road to serfdom*.

⁶³ Nicholls, *Freedom*, pp. 101–2; Hayek, ‘Free enterprise and competitive order’, p. 22 (p. 118 in printed version).

⁶⁴ W. Röpke, *Civitas humana* (London, 1948), pp. 146–7; all in italics in original. See also Röpke, *Gesellschaftskrisis*, pp. 357–61.

⁶⁵ Röpke, *Gesellschaftskrisis*, pp. 266–7, 360.

⁶⁶ Popper, *Open society*, II, pp. 169–70, 318 n. 10; M. Polanyi, *Full employment and free trade* (Cambridge, 1945), pp. 142–5.

Cabinet Office, also endorsed moderate forms of Keynesian intervention.⁶⁷ Robbins, in particular, had extensively revised his views: in the 1930s he had offered staunch opposition to Keynes's advocacy of a government-sponsored reflation of the economy, but he came to doubt the wisdom of this stance during the war. Having seen at first hand the role played by the state in eliminating mass unemployment through war-time expenditure, Robbins became more sympathetic to certain Keynes-influenced policy prescriptions. In this new mood, he and Jewkes helped to draft and promote within government the 1944 white paper on employment policy that famously enshrined the British state's new commitment to maintaining 'a high and stable level of employment'. This iconic document of the British social democratic 'consensus' was therefore shepherded into British public life by two economists who would shortly afterwards take their places as founding members of the Mont Pèlerin Society.⁶⁸ As Robbins later observed in his memoirs, his war-time change of mind had not necessarily led him to endorse everything in the *General theory*; but it did mean that he believed government had an important role to play in smoothing out fluctuations in aggregate demand.⁶⁹

Other neo-liberals presented their ideas as opposed to Keynes's, but like Robbins were also open to the use of government public works and spending to manage levels of demand in the economy. Simons, Hayek, Hutt, and Röpke were perhaps the most vociferous in their criticism of Keynes. But although Simons and Röpke joined with Hayek and Hutt in looking to monetary policy as the best tool to ensure economic stability, both Simons and Röpke actually advocated reflationary fiscal policy as the least worst way of escaping from the depression of the 1930s.⁷⁰ Hayek was, of course, a leading critic of Keynesian demand management in this period. Nonetheless, his differences with Keynes were chiefly technical in nature. There was only one clear allusion to Keynesian economics in *The road to serfdom*. Hayek warned that if attempts were made to even out the economic cycle by funding public works, then 'we shall have carefully to watch our step if we are to avoid making all economic activity progressively more dependent on the direction and volume of government expenditure'. He also noted that he personally favoured the use of monetary policy, rather than fiscal policy, to even out economic fluctuations. 'In any case', he added, 'the very necessary efforts to secure protection against these fluctuations do not lead to the kind of planning which constitutes such a threat to our freedom.'⁷¹ At this stage in his career, Hayek did not view counter-cyclical government intervention as the principal, or even a major, threat to the free society and distinguished between

⁶⁷ Jewkes, *Ordeal*, pp. 63–6, 73; L. Robbins, *The economic problem in peace and war* (London, 1947), pp. 67–73.

⁶⁸ *Employment policy*, Cmd 6527 (London, 1944), p. 3; P. Addison, *The road to 1945* (London, 1975), pp. 242–6; J. Jewkes, *A return to free market economics?* (London, 1978), pp. 39–52; J. Tomlinson, *Employment policy: the crucial years, 1939–1955* (Oxford, 1987), pp. 45–79.

⁶⁹ L. Robbins, *Autobiography of an economist* (London, 1971), pp. 186–9, 224.

⁷⁰ Simons, *Positive*, pp. 34–5; Röpke, *Gesellschaftskrisis*, pp. 279–80; Röpke, *Civitas humana*, pp. 207–8.

⁷¹ Hayek, *Road*, p. 149.

this approach to economic downturns and full-scale economic planning. He later made this even clearer in an unpublished postscript to *The road to serfdom*, written in 1948, where he acknowledged his differences with ‘Keynesian’ analysis, but added: ‘I may be wrong in this. But whether I am right or wrong, the technical reasons for my dissent from the now prevalent view have little to do with the main argument of this book.’⁷²

Most of the neo-liberals, however, deplored the popular version of Keynesian doctrines that began to gain adherents throughout the industrialized democracies in the 1940s. They directed particular animus towards William Beveridge’s *Full employment in a free society* (1944) and the work of the Harvard economist, Alvin Hansen.⁷³ They saw the Beveridge–Hansen version of Keynesianism as mandating an irresponsible degree of state control over the economy and as adopting a target of ‘full employment’ that was far more ambitious, and inflationary, than anything Keynes himself contemplated in the *General theory*. Beveridge stipulated 3 per cent as the unemployment rate at which full employment would be reached, whereas Keynes had thought 5 per cent was probably more realistic.⁷⁴ Neo-liberals considered the Beveridge–Hansen view to be ‘hyper-Keynesianism’ or ‘primitive Keynesianism’, which sanctioned an economically unsustainable, state-directed permanent boom.⁷⁵

IV

The aim of this article has not been to suggest that the characters now labelled as ‘neo-liberals’ were, in fact, new liberals or social democrats in their early years. There is some truth to this claim with respect to a few members of this network, such as Lippmann, Popper, and Polanyi. Aside from these exceptions, however,

⁷² Hayek, ‘Postscript to *The road to serfdom*’, typescript, 1948, Hayek 106–10, p. 12. For a similar interpretation of this evidence, see Shearmur, ‘Hayek, Keynes and the state’, pp. 71–2. Note that Hayek, based in Cambridge during the Second World War, also enjoyed an increasingly friendly personal relationship with Keynes at this time: A. Ebenstein, *Friedrich Hayek: a biography* (Chicago, IL, 2003), p. 106. All of this provides some context for understanding the famously amicable letter that Keynes sent to Hayek after reading *The road to serfdom*: Keynes to Hayek, 28 June 1944, in D. Moggridge and E. S. Johnson, eds., *The collected writings of John Maynard Keynes volume 27: activities 1940–1946: shaping the post-war world: employment and commodities* (London, 1980), pp. 385–8.

⁷³ W. Beveridge, *Full employment in a free society* (London, 1944); A. Hansen, *Economic policy and full employment* (New York, NY, 1947).

⁷⁴ Beveridge, *Full employment*, p. 21; Keynes to Beveridge, 16 Dec. 1944, in Moggridge and Johnson, eds., *Collected writings volume 27*, p. 381; R. Skidelsky, *John Maynard Keynes: the economist as saviour, 1920–1937* (London, 1992), p. 605.

⁷⁵ H. Simons, ‘The Beveridge program: an unsympathetic interpretation’, *Journal of Political Economy*, 53 (1945), pp. 212, 220–2, 229, 233; Nicholls, *Freedom*, p. 52; Röpke, *Gesellschaftskrisis*, pp. 275–9; Eucken to Hayek, 12 Mar. 1946, Hayek 18–40, pp. 1–2; Hayek, ‘Postscript’, p. 13; notes from session on ‘Contra-cyclical measures, full employment and monetary reform’, 7 Apr. 1947, Mont Pèlerin Society meeting, Hayek 81–3. A further concern for neo-liberals was the possibility that this form of Keynesianism would influence the design of post-war international institutions and hence promote a system of co-ordinated international economic planning: for this debate, see J. Toye and R. Toye, *The UN and global political economy* (Bloomington, IN, 2004), pp. 87–109.

there were still sharp differences of principle, policy, and political identity between most neo-liberals and the mainstream social democratic position, as their grave doubts about Beveridge and ‘hyper-Keynesianism’ indicated. While the early neo-liberals rejected *laissez-faire*, they remained more suspicious of the power of the state than their counterparts on the moderate left.⁷⁶ Nonetheless, all the early neo-liberals clearly felt strong pressure from the left not to appear merely reactionary or old-fashioned. The most striking feature of the ideological map in the late 1930s and early 1940s is therefore that, in some respects, the gap between market liberals and the moderate left actually narrowed. Social democrats were increasingly willing to acknowledge the importance of the price mechanism and consumer sovereignty to individual liberty and economic efficiency, while neo-liberals conceded the need for social protection for employees and their dependants; for wealth taxes and public expenditure to ensure a fair start for all; and even for limited intervention in the business cycle during economic depressions.⁷⁷ The neo-liberalism of the 1930s and 1940s was therefore not a fully formed, coherent, and ‘total’ critique of all forms of state intervention in the market.⁷⁸

In stressing that neo-liberals of this period focused on socialism as distinct from what would later be labelled the ‘Keynesian welfare state’, however, I am not suggesting that the attention of neo-liberal writers was fixed on a trivial target. There is no doubt that, partly due to the prestige enjoyed by the Soviet economy, the goal of a post-market order was popular on the left in this period, and that some progressive political leaders and intellectuals had failed to think through the implications of this objective for individual freedom with sufficient rigour. In this sense, many of the points made by authors such as Hayek about respecting consumer sovereignty and freedom of occupational choice were important, well-made, and even found a sympathetic audience at the time among elements of the social democratic left.⁷⁹ But this also reveals that the 1930s and 1940s should be seen as a distinct phase in the history of neo-liberalism. For these self-styled guardians of liberal values, it was a period of immense pessimism, uncertainty, and crisis, much more so than the 1950s or 1960s. Given that so many of the key figures in this nascent movement were from central Europe, this pervasive gloom should hardly be surprising. The post-war settlement was as yet unsettled; the major threats to Western freedom were truly sinister totalitarian regimes. Hayek

⁷⁶ I am grateful to a *Historical Journal* referee for this formulation.

⁷⁷ Nicholls, *Freedom*, p. 87; Tomlinson, ‘Planning’, pp. 157–8, 166–9. This convergence over the role of the price mechanism was noted at the time by Hutt, ‘Economic institutions’, pp. 419–20, but he did not stress the degree to which the ground between the two sides had narrowed on distributive issues as well.

⁷⁸ In reaching this conclusion I therefore dissent from Foucault’s verdict that such a wholesale neo-liberal critique of the state ‘is effectively, completely, and already very clearly formulated in the years 1930–45’: *Birth of biopolitics*, pp. 187–91, quote at p. 189.

⁷⁹ E.g. D. Jay, *The socialist case* (London, 1937); J. Meade, *Planning and the price-mechanism* (London, 1948).

himself later agreed that his target when writing *The road to serfdom* had been 'classical socialism'. Writing in 1956, he noted that he had focused principally on Soviet-style 'hot socialism', at the expense of the cold socialism represented by advocates of the 'welfare state'.⁸⁰

But the surprisingly interventionist character of much neo-liberal thought in this period suggests that this focus on 'hot socialism' was not just the result of a strategic assessment of the most pressing threat to liberal values. Rather, it also stemmed from a belief, common to virtually all of the intellectuals discussed in this article, that the legitimation of the market, and the individual liberty that the market can best secure, had to be accomplished via an expansion of state capacity and a clear admission that earlier market liberals had been wrong to advocate *laissez-faire*. At this stage in their careers, they were keen to demonstrate that their vision of liberalism could accommodate elements of the socialist critique of capitalism. It was in this sense that they were believers in a free economy and a strong state.

⁸⁰ Kresge and Wenar, eds., *Hayek on Hayek*, p. 108; Hayek, 'The road to serfdom after twelve years' [1956], in his *Studies in philosophy, politics and economics* (London, 1967), pp. 220–1.