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Eucken, Hayek, and the Road to Serfdom

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Eucken, Hayek, and the Road to Serfdom

Nils Goldschmidt und Jan-Otmar Hesse
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Eucken, Hayek, and the Road to Serfdom*

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1. Introduction

Walter Eucken (17 January 1891 – 20 March 1950) was the leading and most prominent figure of German liberal economics from the 1920s until well after his death. He represented the convergence between the liberalism of the Austrian school of economics’ “third generation” and the liberal tradition in German economics that gained momentum during the 1930s in opposition to the very strong socialist, national-socialist and romanticist movements in German economics (Goldschmidt and Wohlgemuth 2008; Janssen 2009). Only after the war, when the “ordoliberal” school of economic thought was erected at the University of Freiburg, did this strand of German economic reasoning become influential, especially in German economic policy pertaining to the reorganization of the West-German economy. Though it was influential after the war, the influence of “ordoliberalism” in academia faded out after Eucken’s death in the 1950s, for many reasons (Hesse 2010). Therefore, the similarities as well as the differences between the German and the Austrian schools of liberal thought have remained neglected in the literature.

The differences often appear marginal. They seem to result from the particular historic situation in which they were articulated. But as circumstances evolve over time and fundamental global economic crises return, it is, in our opinion, worthwhile to take a closer look at the differences between these two strands of liberalism, one having been developed within the totalitarian regime of Nazi Germany and the other one ‘in exile’. We think the correspondence between two of the most outstanding figures of the two “schools” of thought might be a fitting starting point for this approach.

In the following we first want to shortly describe the evolution and the nature of the contact between Eucken and the last Viennese generation of the Austrian school of economics. In a second step, we will analyze the differences between the schools following a close reading of a detailed comment by Eucken on Friedrich A. Hayek’s (1944) *Road to Serfdom*, written in March 1946, a few months after a German translation of the book was published. Our examination begins first with a remark by Eucken criticizing Hayek’s neglect of the German liberal tradition. Finally, the third chapter of the article deals with Eucken’s observations that highlight the minute yet significant differences between the two approaches of (Neo)Liberalism.

2. Eucken’s position on international liberal economics and his relationship to Hayek

The relationship between the German liberals, later to become the “Ordoliberals”, and the Austrians, later to become the American neoliberals, did not actually result from the famous symposium organized by Walter Lippmann in Paris in 1938 – as the story often has been told (Foucault 2004 [1978]). In fact, the modest re-union of the younger scholars after the “Methodenstreit” (debate over methods) started much earlier, during the annual meeting of the *Verein für Socialpolitik* that was held on the question of business cycle theory in Zurich in 1928. (Blümle and Goldschmidt 2006; Köster 2011). Then, younger Austrians like Fritz

* All translations of original German sources by Sigrid Saou. The authors thank Uwe Dathe and Hansjörg Klausinger for their helpful comments and suggestions.

Machlup and Gottfried Haberler met with marginalized younger liberal economists from Germany, scholars such as Eucken, Wilhelm Röpke, L. Albert Hahn and Georg Halm.¹

It is important to understand that the history of post-war economic liberalism in Europe resulted from the pre-war relationship between “the Austrians” and the small group of German liberal economists, which led to the foundation of the Mont Pelerin Society (MPS) shortly after the war. We are not yet able to precisely date the starting point nor determine the nature of the early contacts between Eucken and Hayek. The earliest letter by Eucken to Hayek that is held by the Hoover Institution dates back to 1939 – but was probably not the first one written.² Correspondence between Eucken and Machlup, another important figure in the relationship, starts in 1934: Machlup, then a 32-year old Rockefeller Fellow studying in Chicago, had sent a copy of his book on the economic crisis to the then well-established and influential Freiburg professor of economics, son of the 1908 Nobel Prize laureate in literature, Rudolf Eucken, and he received a polite thank you note in response.³ Eucken’s early correspondence with Hayek was dedicated to philosophical questions related to Hegel and Marx.

The character of the correspondence changed after the war: Remarkably early, only three months after the German surrender, Eucken wrote to Hayek inviting him to Freiburg in order to promote the liberal ideas outlined in *Road to Serfdom* and to fight against the threat of planning and socialism: “It is of the utmost importance that those who are determined not to follow the ‘Road to Serfdom’ remain in contact, in close contact. May you come to Freiburg? To give a talk perhaps?”⁴ “We non-socialist economists must cooperate across borders. The helplessness in which practical economics finds itself requires this.”⁵ In the correspondence between Eucken and Hayek, the plan to erect an international organization composed of liberal economists and activists was discussed as early as January 1946. And when the MPS was finally established at the famous meeting that took place in April 1947 in Switzerland, Eucken was the only participant from Germany. After Hayek became the first president of the MPS at the first meeting, he always consulted Eucken before inviting any German thinker to join the association. However, Eucken recommended that a rather careful policy be applied in this respect. In the summer of 1947, he suggested inviting only law-professor Franz Böhm, his old faculty colleague Constantin v. Dietze, entrepreneur Walter Bauer, and his two pupils, Karl Friedrich Maier and Bernhard Pfister (later to become professor of economics in Munich).⁶ He explicitly advised against inviting Alfred Müller-Armack, then professor of economics in Münster, who coined the term Social Market Economy and later became an

¹ Ludwig v. Mises (1978, 102) wrote the following passage about that meeting in his memoirs: “That these men were no economists we must not hold against them. After all, they were the pupil of Schmoller, Wagner, Bücher and Brentano. They did not know the economic literature, had no conception of economic problems, and suspected every economist as an enemy of the State, as non-German, and as protagonists of business interests and of free trade. Whenever they examined an economic essay, they were determined to find deficiencies and errors. They were dilettantes in everything they undertook.” But among others, Eucken, Röpke, Hahn and Halm were excluded from that judgement.

² Eucken to Hayek, 27.6.1939, Hoover Institution Archives (Stanford University Palo Alto, hereafter abbreviated as: “HIA”), Friedrich A. v. Hayek Papers (hereafter: “FAH papers”), Box 18, Fo. 40.

³ Eucken to Machlup, 25.2.1934, HIA, Fritz Machlup Papers, Box 36, Fo. 16

⁴ Eucken to Hayek, 12.8.1945, HIA FAH Papers, Box 18, Fo. 40 (our translation).

⁵ Eucken to Hayek, 10.11.1945, HIA FAH Papers, Box 18, Fo. 40 (our translation).

⁶ Eucken to Hayek, 26.8.1947, HIA FAH Papers, Box 18, Fo. 40.

influential advisor to the German minister of economics, Ludwig Erhard. He suggested including two leading figures from the staff of the Frankfurt administration of economics instead.⁷ Eucken apparently served as a kind of gatekeeper in the opening of German liberal circles to international discussion. Even the inclusion of the German minister of the economy into the international community of liberal economists and entrepreneurs was discussed with Eucken beforehand.⁸

The early correspondence highlights the fact that Eucken was perceived as an academic authority and respected colleague, not as a victim of National Socialism that needed the help of foreign scholars.⁹ It was Hayek who suggested to Eucken to prepare an English translation of his textbook *Foundation of economics* and offered his help in finding a publisher.¹⁰ Most of the letters exchanged dealt with organizational issues – as described above. Therefore, the letter we wish to turn to now is an exception in that it is a seven-page detailed discussion of Hayek's *Road to Serfdom*. Hayek had asked Eucken for a detailed examination of the work, especially to help him locate quotations from German literature that were difficult to access in English libraries.¹¹ Though Eucken's answers contain little in that respect, they offer a good opportunity for analyzing the differences between Hayek and Eucken's approaches to economic policy.

3. Eucken's idea of a German tradition of liberalism

Eucken introduces his discussion of the *Road to Serfdom* as incomplete and apologizes for the fact that he did not have the time to think about the book in depth, as he would have liked to. His discussion is divided into seven points. All his comments pertain to the first translation of Hayek's (1945) book by Eva Röpke, published in Switzerland in 1945. Eucken's comments in his last point are different from the preceding six: Whereas the other six discuss particular points of Hayek's arguments, the seventh comes as a history of German liberalism that, in Eucken's view, needs to be added to Hayek's story. Furthermore, it allows Eucken to depict his own intellectual tradition. This is why we start by examining the seventh point of Eucken's letter – as well as the persons mentioned in it and the idea of German liberalism as perceived by Eucken – before moving on to a more detailed analysis of the other six points. In our opinion, the fact that Hayek did not mention the German tradition of liberal economics is much more than simple lack of knowledge. It is probably intentional in that Hayek did not perceive the scholars mentioned by Eucken as liberals. The intellectual traditions of Eucken and Hayek differed significantly, which might explain some of the differences in their approaches.

⁷ His former pupil and assistant in Freiburg, Leonhard Miksch, and Heinrich Rittershausen. Eucken to Hayek, 5.4.1948, HIA FAH Papers, Box 18, Fo. 40.

⁸ Eucken to Hayek, 3.2.1949, HIA FAH Papers, Box 18, Fo. 40.

⁹ Hayek asked Eucken for help in the denazification-trial of his brother, Heinrich v. Hayek, who had occupied the position of associate professor in medicine at the University of Würzburg during the war. He was suspended in 1946 and had received a call to the University of Freiburg some months later, which was then threatened by the de-nazification committees' decision. (Hayek to Eucken, 1.2.1947, HIA FAH Papers, Box 18, Fo. 40).

¹⁰ In his answer Eucken wrote to Hayek that he had given the rights for any English translation of his *Foundations* to his pupil Friedrich A. Lutz in the summer of 1939, when the war broke out. Eucken to Hayek, 22.11.1947, HIA FAH Papers, Box 18, Fo. 40.

¹¹ Hayek to Eucken, 8.2.1946, HIA FAH Papers, Box 18, Fo. 40.

Eucken's critique of Hayek's description of the history of German political thought since the late 18th century refers to chapter 12 of the *Road to Serfdom*. Though Hayek (1945, 210) started this chapter mentioning that some of the "socialist ideas" that fuelled the *Road to Serfdom* also appeared in English and French political thought, he believed that German authors had been "leading" in that respect. He started his overview of German literature with Werner Sombart's book *Händler und Helden* ('Traders and Heroes'), a direct attack on the liberal idea of individual freedom. Eucken considered Hayek had exaggerated Sombart's influence on German political thought. Furthermore, he believed Hayek overestimated the influence of Johann Plenge, economist at the University of Münster, whom Hayek quotes intensively (Hayek 1945, 215f). Plenge was, in fact, perceived as an outsider by many serious German economists (see Köster 2011, 176). Eucken was of the opinion that Othmar Spann had been more influential than Plenge, yet Hayek did not mention him.¹² In general, Eucken supported Hayek's view according to which the idea of a socialist economy – or "centrally-planned economy" in Eucken's term – had gathered momentum in Germany in the 1920s and had been infused with nationalist, and later on racist, ideology in the so-called "conservative revolution" and in the writing of the *Tatkreis* (literally translated as "action circle"), which Eucken mentions at the very beginning of his letter. The *Tatkreis* called for an end to capitalism, while promoting a neo-mercantilist ideology based on private property, a system that encouraged exports and discouraged imports, promoting German self-sufficiency. The typical economic ideology was to combine the advantages of a market system with the centralized control of all economic action. Though the circle's journal *Die Tat* (Action) remained comparatively small in terms of circulation, its ideology was influential for it was used as a model for the economic reasoning of the Nazis, who then dissolved *Tatkreis* in 1933 (see Barkai 1988, 92).

Eucken, however, aimed at strengthening another strand of German economic thought that Hayek had broadly ignored. There had always been an opposing strand of intellectual tradition in Germany to counter what Hayek called the "neo-German" intellectual tradition: "a classic movement and a romantic movement had developed side by side", as Eucken puts it in his letter to Hayek.¹³ Eucken believed that more attention should especially be paid to the liberal strand of economic thought that "was forced into the catacombs" during the decade of National Socialism. He then briefly mentions some names who, in his opinion, had been important figures of this tradition: The Königsberg professor of economics, Christian Jakob Kraus, was the earliest and most prominent interpreter of Adam Smith in Germany in the late 18th century and became very influential because he trained a whole generation of distinguished Prussian civil servants (Wehler 2011, 35) who initiated liberal economic reforms in 1809/1811, with the introduction of free markets and the individual freedom of peasantry. The next name that Eucken mentions as a milestone of liberal thought in Germany does probably refer to the liberal politician Rudolf von Delbrück (1817-1903), who acted as the head of the Bismarck-administration in Imperial Germany and propelled the turn to free trade and liberal economic reforms before he was dismissed during Bismarck's switch to protectionism in 1876.

The Göttingen and Freiburg economist Hans von Mangoldt (1824-1868), whom Eucken mentions as a third figure of German economic liberalism, is probably much better known to historians of economic thought. Although he is generally portrayed as a German 'classical' author, he anticipated 'neoclassical' ideas: Schumpeter's theory of the entrepreneur, Alfred Marshall's partial price analysis and the graphical representation of supply and demand.

¹² Hayek spent three pages on an analysis of Paul Lensch, who played no role in that strand of thought, but Eucken did not comment on that.

¹³ Eucken to Friedrich A. Hayek, 12.3.1946, HIA FAH Papers, Box 18, Fo. 40, our translation.

Mangoldt remains closely tied to the classical tradition, but he introduced mathematical representations that point to the neoclassical direction. It is remarkable that Mangoldt's contemporaries did not pay much attention to these theoretical developments. Mangoldt's most interesting mathematical ideas were even omitted in the posthumous editions of his principal work. The fourth name given by Eucken is Heinrich Dietzel (1857-1935), professor of economics in Bonn and considered an "academic loner". He was neither a follower of the mainstream Historical School, nor did he advocate the tenets of the Austrian Marginalism School – rather, he attempted to follow his very own line, which was based on the roots of classical theory. He "was a lone epigone of Classical economics" – as von Mises (1969, 3) puts it. He occupied the middle ground with regard to the theory of value, an issue on which he had fiery debates with Eugen von Böhm-Bawerk. Dietzel tried to unify the objective and subjective theory of value by aiming to prove that utility (*Nützlichkeit*) is the common precondition of marginal utility theory and classical theory. And – of course – he is important because Eucken studied with him during his time in Bonn (Kasprzok 2005; Goldschmidt 2002). Eucken wrote to Hayek that when he argued with the promoters of the "socialist" tradition, Arthur Moeller van den Bruck and Oswald Spengler, these were the people his opponents always quoted as their enemy thinkers.

Eucken considered himself and a group of colleagues named "the younger generation" to be part of that tradition and indicated that even under National Socialism he and some colleagues had been able to put forward liberal economic reasoning in official meetings, e.g. with the Commissioner for price regulation in 1941, where Eucken's ideas were supported rather than opposed. In a previous letter to Hayek, Eucken had already described what he calls a "curious event": one of the members of the Freiburg circle, the Cologne economist Günter Schmolders managed to organize a conference on the question of competition in the "lion's den", namely the administration for price regulation.¹⁴ He also named Heinrich von Stackelberg, Hans Gestrich and August Lösch as part of this group of liberal and market-oriented economists. The existence and the influence of this small group of liberal economists in Germany was broadly confirmed by recent historical research. Hauke Janssen even speaks of "German Ricardians", a term that appears in the correspondence with Alexander Rüstow but might have been overestimated by Janssen (Janssen 2009, 38; Köster 2011, 227). Nevertheless, liberal schools of thought continued to exist in Germany during the 1920s and the 1930s (Ptak 2004; Nicholls 1994).¹⁵

However, the German liberalism that Eucken had in mind was based on more modest – yet essential – conceptions compared to the Anglo-Saxon tradition Hayek reflected upon. German "liberalism" in the 1930s (and this applies to Eucken as well) did not perceive market competition as a mechanism that would take over when state intervention was absent. To German liberals state initiative was inevitable since they believed that without it, in some cases, competition would not occur. Furthermore, German liberals (such as Eucken) analyzed

¹⁴ Eucken to Hayek, 8.2.1946, HIA FAH Papers, Box 18, Fo. 40. The contributions to the conference were later published by Günter Schmolders (1942). In his memoirs, Schmolders (1989, 72) described the organisation of the conference as well as the publication of the volume as an act of opposition against the Nazi regime though "competition" cannot in itself be treated as anathema to Nazi ideology (see Hesse 2006). On the resistance of the Freiburg circles in general see Goldschmidt (2011).

¹⁵ Perhaps somewhat bold in this respect is David Gerber's (2003, 232) introduction to the contribution of the Freiburg School to the development of international competition law: "intellectual impulses for the extraordinary reversal of direction in social and political development [...] came not from a traditional liberal bastion such as England, but from the territory of a recent enemy of liberalism: Germany".

the economy with a view to increasing welfare rather than to improving individual freedom, which they believed would mainly strengthen private power. The fact that Eucken and Hayek proceeded based on two opposing premises, though not explicitly mentioned in the letter, might explain why Hayek ignored this German tradition of liberalism, as he would have perceived it as being close to “collectivism”. Eucken and Hayek clearly had a very different understanding of the relation between freedom and order.

4. Different approaches to liberalism

When focusing on the differences between Eucken and Hayek’s positions, it becomes clear that the seven points of Eucken’s letter overlap on several issues, which is why we have reorganized our analysis into three parts: We will first address the issue of social order vs. individual freedom, then the conditions and meaning of competition and finally the relationship between socialism, democracy and liberalism.

4.1. Social order vs. individual freedom

In his discussion about the principles of economic order in his letter to Hayek, Eucken (1926, 15, our translation) writes: “But in truth, it is a serious matter that the person who is the most efficient at circumventing the legal order is always the one who fares best.” This statement is fundamental in understanding what distinguishes ordoliberalism from the Anglo-Saxon brand of liberalism. In his writings, Eucken focuses not only on the question of a legal order as a prerequisite for competition, but he connects this idea with his considerations on a “comprehensive intellectual order of life.” Even though Eucken’s (2004 [1952], 184, our translation) terminology changed later on in his academic life, the objective of his research remained the same and is succinctly summarized in his *Grundsätze der Wirtschaftspolitik*: “We need to get used to the idea that solemn questions about the intellectual and spiritual existence of Man have to be combined with rather sober and mechanical issues of economic design.” ‘Order’ was Eucken’s yardstick for economic policy. Pursuing a venerable tradition, which spans Augustine, the medieval thinkers and the Physiocrats, Eucken (1989 [1940], 239, our translation) is in search of the order that “conforms to the reason or nature of Man and things”. While Eucken (2004 [1952], 347, 373, our translation) abstains from “immediate derivations from natural law” – a fact which is hardly surprising given his phenomenological methodology (Goldschmidt 2012) – the competitive order that Eucken strives for is “in another sense [...] a natural order or *Ordo*”. In this spirit, he details how a competitive order “brings to the fore those strong tendencies which, in the industrial economy as well, push towards perfect competition. Economic policy, by making these tendencies effective as elements of order, does what corresponds to the nature of things and of Man”.

Thus, the goal is an economic policy guided by principles and corresponding to an ideal order. In this perspective only can one appreciate Eucken’s (2004 [1952], 240, our translation) harsh criticism of the “experimental economic policy” of the past decade: “We therefore face the great task of providing this new industrialized economy, with its far-reaching division of labor, with a *functional* and *humane* order of the economy”. Compared with an Anglo-Saxon type of liberalism, the notion of freedom is secondary to the notion of order: freedom plays no fundamental role in Eucken’s concept. This is why freedom has no significance in the *Foundations*, first published in 1940; only in the posthumously published *Grundsätze der Wirtschaftspolitik* does it take centre stage. Freedom, for Eucken (2004 [1952], 370, 179, our translation), is not a value in its own right, and Eucken’s call for a “program of freedom” does not aim at making freedom absolute. Rather, Eucken’s *ordoliberal* approach explains his understanding of freedom, which is another way of saying that this notion is important to

Eucken because the order that is to be realized must guarantee freedom: “The crucial question is: what types of order warrant freedom”. Hence, the notion of order is constitutive of the notion of freedom and that might explain why Eucken emphasizes in his letter to Hayek: “Indeed, the right way is a third, new way.” Eucken’s comments on the different types of competition law may illustrate that difference in a more concrete way.

4.2. The Conditions and Meaning of Competition

Competition and concentration of economic power is treated at different points in Eucken’s comment. His second remark is concerned with the general process of industrial concentration described by Hayek (1945, chapter1). While Hayek (1945, 73ff) emphasizes the role of economic policy in the emergence of big business and concentration, Eucken argues that big business did not necessarily result from the growth of enterprises heading for economies of scale, but from collusion in a broad and general way. Corporate law, taxes and the protection of brands would have fuelled that process according to Eucken. Therefore, state intervention and the failure to regulate contribute to the process of concentration of business. In his third point Eucken reflects on the role of patent law: In a minor footnote in chapter 14, Hayek (1945, 252) wrote that, in his opinion, cases where people resorted to a patent in order to prevent competitors from using the patented innovation, without using it themselves, were rare occurrences. Eucken, however, believed such cases to be more frequent. Hayek’s footnote might sound as though he defends that practice, but Eucken assumes that the reduction of patent law and especially of its negative effects would be an important aim for both of them. Eucken also addresses economic power as personal motive in the business elite of private firms in his point 5. He was of the opinion that the erection of a competition-based order (*Wettbewerbsordnung*) would dissolve that negative effect of capitalism as well.

It is on this point that Hayek and Eucken’s positions diverge the most, even though the disagreement is not explicit and is only to be found in a few detailed remarks. In Eucken’s case, issues relating to cartels and monopoly took on a very concrete dimension when he was asked by the French occupation authorities, at the beginning of 1946, for his expert opinion on legislation aimed at preventing the concentration of economic power as part of the allied demerger and decartelization policy. The principles that he developed in this regard were first published in a summary fashion in the *Ordo* Yearbook of 1949. They were to be the foundation of the German “Act against Restraints of Competition”, which – due to several years of internal political fighting – was not adopted until 1957. Eucken believed that economic positions of power that interfered with competition should in any case be restricted or forbidden by law. Only in very few cases did he think there were no other means of supply to the population than through a monopoly. In these rare instances of “unavoidable monopolies”, independent oversight bodies should be set up in order to limit the abuse of monopoly power. Though Hayek did not have a definite position regarding antitrust law at the end of the 1940s, after Eucken’s death he clearly moved towards the early Chicago Schools’ line of thought as well as Ludwig von Mises’. The latter had openly confronted Eucken during the first meeting of the MPS, arguing against any form of legislation regulating market agreements (Plickert 2008, 198-206; for a general discussion on Hayek, Chicago and Freiburg see: Köhler and Kolev 2011).

Even though at the beginning of 1946 Eucken agreed with Hayek (1945, 67) about the fact that business concentration was not an automatic outcome of capitalism but instead could be traced back to wrong choices in state intervention, he nonetheless advocated state regulation of economic power and viewed a competition-based order as a solution. Contrary to Hayek, in 1946 he was reluctant to view market imbalances and oligopolies as being the temporary consequences of an adjustment process. Already in 1940, in *The Foundations of Economics*,

Eucken (1950 [1940], 146, 120) had strongly rejected the established terms of “imperfect competition” or “monopolistic competition” used to describe these phenomena: “It is in the interests of economic pressure-groups to confuse the distinction between competition and monopoly. The effect of monopolies are shown to be harmless and the special problems of economic constitutional law which the existence of such powerful private bodies creates, are concealed”.¹⁶

Given that Eucken only marginally addresses the issues of concentration and monopoly facilitation through patent, tax and corporate law in these letters, it is not possible to work out a detailed analysis of the fundamental differences between Hayek and Eucken on these issues at that time, contrary to what could be done based on later publications (Plickert 2008; Woll 1989). Rather, these 1946 excerpts highlight a particular aspect revealed by this correspondence: whereas in his *Road to Serfdom* Hayek focuses mainly on the intellectual history of Liberalism and its opponents, Eucken’s comments are already the words of a political advisor dealing with day-to-day operations – a man who, when addressing antitrust law, is no longer thinking in theoretical terms but in view of the concrete problems facing Germany’s competitive order.

4.3. Relationships between Socialism, Democracy and Liberalism

Eucken’s remarks about socialism, democracy and liberalism in his letter to Hayek are, in a way, surprising. On the one hand he criticizes the quote by Tocqueville included by Hayek in his book as being inadequate and not really relevant to the distinction between socialism, democracy and liberalism. In *Road to Serfdom*, Hayek (1945, 45) quotes the following passage by Tocqueville, addressed by Eucken in his letter: “Democracy extends the sphere of individual freedom [he said in 1848], socialism restricts it. Democracy attaches all possible value to each man; socialism makes each man a mere agent, a mere number. Democracy and socialism have nothing in common but one word: equality. But notice the difference: while democracy seeks equality in liberty, socialism seeks equality in restraint and servitude.” Eucken responds: “To sum up, here is how I understand it: socialism and democracy are incompatible. Second, socialism and liberalism are incompatible. Yet liberalism and democracy are not identical. There also exists, as you yourself show, democracy without freedom. Consequently, socialism is incompatible with two different things, namely democracy and liberalism.” On the other hand, Eucken stresses that this latter position is also to be found in Hayek’s *Road to Serfdom*, pointing to the last two pages of the chapter ‘Planning and Democracy’, in which Hayek describes democracy as a means of safeguarding inner peace and individual freedom. However, according to Hayek the only objective and end to be pursued is liberty. Indeed, although a democratic regime counters dictatorial systems, democracy can also lead to arbitrariness and thus to the annihilation of individual freedom. Therefore, what is needed to prevent arbitrariness and to safeguard individual freedom is not rational democratic choice *per se* but an effective limitation on governmental power.

Against this background, it would seem that there is in fact no disagreement between Eucken and Hayek. Why, then, does Eucken raise this topic in his letter and indicate: “I should, however, write again in more detail on that subject and particularly tell you of the German experiences”? This sentence alluding to further discussion shows that for Eucken, it is about

¹⁶ Karl Steinbrück, in his 1954 dissertation, supervised by Heinrich von Rittershausen, argues that Eucken ignored the international debate. Ernst Heuss (1986) also links this dissociation to the isolation of German economic sciences during the war. Heinrich von Stackelberg (1940, 266), however, wrote as early as 1940 that “Eucken did not ignore this distinction [between perfect and imperfect markets]: he expressly rejects it in an argument with Chamberlin and Robinson.”

more than just an inadequate quote by Tocqueville. Rather, Eucken's comments reveal an uneasiness that should not be treated as insignificant towards an exaggerated trust in democracy as the necessary counterpart to a liberal order. This skepticism reflects his experience of the Weimar Republic and it is no coincidence that Eucken did not directly address the question of democracy even in his posthumously published *Grundsätze der Wirtschaftspolitik*. In the two passages where he discusses democracy, he does so through quotations. He quotes the *Economist* with the following statement: "If liberal democracy is not compatible with full employment, then it must disappear", a position that Eucken (2004 [1952], 140, our translation) fully supports. In another passage, he quotes Keynes who, in 'The End of Laissez-Faire', mentions the possibility of corporations within a democracy – a concept towards which Eucken (2004 [1952], 244, our translation) was very critical.

It would, however, be a mistake to describe Eucken and Ordoliberalism as being undemocratic or even antidemocratic on account of this skepticism towards democracy, even though it is a view regularly found in the literature (Kirchgässner 1988; Haselbach 1991; Ptak 2004; Ptak 2009) and often associated with a concept that Eucken, Böhm and others often referred to, that of a "strong state". Eucken's (1932, 308, 303, our translation) reasoning is in fact quite different: Ordoliberals oppose "interventionist state capitalism" ("*interventionistischen Wirtschaftsstaat*"), a weak set-up when it comes to safeguarding the economy against privileges, particular interests and the ideologies they carry with them, thus undermining its own authority. Instead, they advocate a strong state that is able to counter the lobbying of individual groups and allow for a general order that is beneficial to all. This does not mean "politicizing the economy" but rather establishing a few principles that will then build a framework within which market forces can freely unfold. This concept finds its classical form in the idea of constitutive principles, as outlined by Eucken in *Grundsätze der Wirtschaftspolitik*. It is a matter of establishing a stable economic and social structure that is committed to safeguarding the freedom and dignity of all members of society. A "strong state" in this sense cannot be equated to a totalitarian state that (as its objective of societal development) increasingly intervenes in the private sphere of its citizens and attempts to guide them; rather, it is an effective state that serves the aims of society (as an instrument). Such an effective state imposes clear and general rules regarding order on the economy in order to safeguard the social function of market competition as a decentralized coordinating process for individuals who enjoy equal rights/on an equal footing. Any form of socialism is to be rejected because it ultimately fosters economic and social centralization and leads to a concentration of economic power. The Ordoliberals, however, remain vague as to their position regarding other forms of government and the role of democracy in safeguarding societal order is considered minor.

Hayek on the other hand has a very different approach: For Hayek (2002 [1965], 124, our translation) – and this applies to his later writings too – democracy is crucial in its role as a potential barrier against the repression of individual freedom. In his opinion, the threat posed by democracy is not – as Eucken would have it – the fact that it might be impossible to establish a functional and humane economic order, but rather that democracy itself might degenerate if it is not limited by the rule of law: "All the places where democratic institutions were not kept in check by a vibrant tradition of the rule of law and degenerated quickly into 'totalitarian democracies' or even 'plebiscitary' democracies should make us realize that what is actually at stake here are not particular institutions but certain more profound underlying convictions [...]." Hayek advocates a constitutionally limited democracy, i.e. a constitutional liberalism "that focuses on the need to respect the principle of individual sovereignty at the level of constitutional choice." (Vanberg 2011, 3; see also Vanberg 2008)

To recapitulate: A comparative analysis of political structures as viewed by Eucken and Hayek shows that the heart of the matter is the relationship between freedom and order.

Ordoliberals basically conceive a liberal, i.e. free, society as a society devoid of any concentration of powers, defying both economic and political totalitarianism. In order to achieve this, stable state-run structures are necessary and precede the unfolding of liberty. For Hayek, however, in line with the Anglo-Saxon tradition of liberalism in general, a liberal society is first and foremost characterized by the possibility to exercise individual freedom. In this perspective, any form of socialism is considered a great evil, whereas democracy can serve this purpose, as long as it is itself bound by general rules.

5. Conclusion

After the Second World War, Eucken and Hayek were perhaps the two most significant proponents of economic liberalism in Europe. Not only were they both particularly influential in the political debates in their respective countries, but they were also united in their active hostility towards socialist economic policy, which they jointly strove to thwart. To that end, they found ways to start corresponding right after the German capitulation and also cooperated closely in the founding of the MPS in 1947. Though our endeavor in this foregoing discussion has been to emphasize the differences between both thinkers' intellectual positions, we must not lose sight of the fact that we are addressing nuances between two variants of liberalism, which, given their common stance against socialist thinkers back then could only be rudimentarily distinguished one from the other. The unifying elements in Eucken and Hayek still, to this day, clearly outweigh the differences, and any statement according to which, had socialism been pushed back, the differences would have emerged more clearly, remains pure speculation.

Moreover, the differences are due to the fact that in 1946, when Eucken discussed *The Road to Serfdom* in his letter to Hayek, the personal circumstances and the lines of thought followed by both thinkers could hardly have been further from one another: while Hayek, through the publication of his book in England and his lecture tours in the USA, had become a public intellectual figure in those countries and mainly concerned himself with the academic issues discussed in this milieu, Eucken was one of the most prominent economic policy advisors in post-war Germany and was concentrating on the very concrete political economic problems faced by a "society in ruins". This explains why Eucken, in his remarks, puts forward a more down-to-earth and political argumentation.

Nevertheless, within this framework, we could already recognize in Eucken's detailed remarks – from 1946 – about Hayek's *The Road to Serfdom* some fundamental differences between the two liberal positions. Simply the depiction of his own intellectual path indicated that Eucken, contrary to Hayek, did not trace his brand of liberalism directly back to the British tradition following Adam Smith, but rather perceived it as being the continuation of an idiosyncratic "German" liberalism. We presented three main points in which we addressed the – sometimes admittedly very subtle – differences found in the 1946 letter:

1. Eucken's conception is based on a representation of societal order that, in his opinion, must prevail over individual freedom.
2. This had a direct impact on his position regarding cartels. He believed that it was necessary to prevent the creation and abuse of power concentration by resorting to state authority. Hayek, on the other hand, tended to reject such intervention in competition and later even publicly opposed a ban on cartels.
3. Eucken's comments repeatedly point to a crucial disagreement, though it is only feebly hinted at in the letter, when dealing with the relationship between political system and economic system: While Eucken assigns to the state the role of organizing competition,

Hayek believes that competition is more or less an economic natural state requiring a substantial absence of state intervention.

We believe it is significant that these differences in basic assumptions regarding economic liberalism can already be recognized in the difficult circumstances of 1946, at a time when both parties professed the greatest possible interest in international cooperation between proponents of liberalism. And given the current crisis facing liberal economic policy, these differences are perhaps important enough for them to be addressed once again.

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Appendix:

Walter Eucken to Friedrich A. Hayek, 12.3.1946, HIA FAH Papers, Box 18, Fo. 40.
(Translation from original German).

Professor Walter Eucken

Freiburg i. Br., March 12, 1946

Goethestr. 10

Professor F.A. Hayek

London School of Economics

Houghten Street

Aldwych

London WC 2

Dear Mr. Hayek!

I hope you have by now received the latest edition of my work, *The Foundations of Economics*, with the letter included. – It is a pity that we can not get together in the next few months. There would not only be plenty to discuss with regards to the situation in Germany and in the world, but there would also be plenty to say concerning many scientific issues. When one, which is our case, has been cut off from the rest of the world for so many years, it is absolutely necessary to quickly re-establish full contact with the intellectual work being pursued outside of our borders. I have here at the moment several scholarly works that are already well advanced, and I also would have liked to discuss them with you. Today, however, I would like to write a few words about your book. Of course these are only preliminary remarks since these past few months I have been caught up in many activities and have not had the peace and quiet I would like to reflect in depth on all this.

As I have already written, I quite agree with your book, and at the same time I have learned a lot reading it. The evidence showing that the English development follows the German one with a certain lag is especially convincing, though it is also depressing. I had already noticed signs pointing to these facts. For instance, Carr's book, which became famous here during the National Socialist era and which is strongly reminiscent of the ideas of the *Tatkreis* ("Action Circle"). But voices apparently coming from the liberal side also sounded worrying. For instance, the fact that the Beveridge Plan was included by the Liberal Party in its platform. Or the position of the Economist on the issue of full employment, for example. All this, as well as Keynes' influence, shows a certain ignorance with respect to the formidable risks posed by this development, risks that we experienced first hand in their entirety. (By the way, your book has encouraged me to describe the German experiences, which I have observed very closely, in a systematic way. This also applies to the problem of economic calculation in a centrally-planned economy. The difficulties that had been identified in theory have now appeared in reality and have critically compromised the functioning of central economic planning. Schumpeter should have taken such experiences into account, though we are only acquainted with his book through discussions). Your book, however, is the first to fully depict the tragic situation. In this respect, chapter thirteen is particularly convincing; and one may only hope that this book will help England take stock of the situation and help the English clearly understand that England, especially now, has a historic mission; the English, who are about to renounce this mission.

May I now bring forward a few points for discussion, things that crossed my mind as I was reading:

1. On page 66 you discuss the translation of the necessary planning which is required to make competition a beneficial competition in performance. And on page 37 you underscore the difference between a competition-based order and laissez faire. Wouldn't it be appropriate, however, to mark this difference more strongly. I enclose a few drafts that I wrote in which there is a particular stress on this opposition. (You can also see that in this one unpublished report the publisher mentioned your book). Now, after decades of economic policy administered in this way, the process of concentration is so advanced in most industrialized countries that introducing laissez faire would lead to some economic agents gaining too much power, it would lead to monopolistic, partly monopolistic or oligarchic market forms, to imbalanced markets and to social struggles. Then it would

once again be necessary to have state interventions, and in a short period of time centrally-planned interventionist methods would once again dominate economic order. It is therefore critical, from the beginning, to push for a real competition-based order. – Even though the purpose of your book is not to examine in detail the necessary measures to achieve this, one could perhaps nonetheless outline the most fundamental elements in a few pages. Indeed, the right way is a third, new way.

2. On a related note, a few remarks concerning your fourth chapter, especially on the issue of concentration. You rightly argue against the idea according to which there is a technical reason for the rise of monopoly. Shouldn't one however also note the following: the real process of concentration has nothing to do with the growing size of the company, instead, it has to do with the fact that through the formation of consolidated companies, trusts and cartels, the management of the company, or the market supply, ends up in the hands of one or a few people, who, thus, become monopolists or oligopolists. In this way, a consolidated company, or a trust, or a cartel, usually comprises many, sometimes hundreds, of businesses. Thus, research into the so-called optimal size of a business only marginally deals with the problem of concentration and monopoly. And linked to this, the fact that non-technical causes played a decisive role in industrial concentration; this is also true for modern corporate law, especially with respect to stock companies, for patent law, including licencing law, for the protection of trademarks with the protection of resale price maintenance. It is also true for tax law, for instance the sales tax. This lead to two different things: First to the totally unwarranted centralization of the management of several businesses into the hands of one person, and second, to the fact that ultralarge business sizes were chosen, i.e. business sizes that exceeded the technical requirements. This excess can be observed not only with consolidated companies, but also everywhere with the unions and their quota battles.

I think that it would be appropriate if you dwelled a little more on the true character of the movement of concentration and of monopoly. By the way, there are many very interesting remarks in Haussmann's book on "The economic concentration and its reversal of fortune", published in 1940, though I may not agree on other points in the book.

3. On a related note, an observation about the remark on page 252. The occasional destruction of wheat etc. can of course not happen in the market form of full competition.

But shouldn't one add that this destruction of supplies is a phenomenon that typically occurs in a supply monopoly and – this can easily be shown – can only take place in monopolistic or partly monopolistic market forms.

With respect to the non-utilization of valuable patents, this is something that occurs quite often. We have dealt with these problems extensively, and I hope I will soon be able to send you the work of one of my students on that subject. Current patent law is one of the main culprits for the formation of consolidated companies and monopolies and imperatively needs to be reformed so that an adequate competition-based order can emerge. What I mean is that we should not defend the cases of non-utilization of valuable patents, rather, from these cases, we should draw the conclusion that a definitive reduction of patent protection (which is in its essence monopolistic) is required.

4. About your sixth chapter: we in Germany have experienced how incompatible a planned economy and the rule of law are. Consequently, it might be possible to illustrate this excellent chapter with cases from the German experience.

The fact that the notions of law and justice were already undermined played a decisive role in the elimination of the rule of law. But then, with the expansion of the centrally-planned economy, came the economic policy effects. They were first seen in the fact that with the centrally-planned economy, the administration obtained an unbearable ascendancy over legislation. For instance, in this way, a comprehensive piece of legislation was issued to protect the crafts. But because the central planning agencies needed workers, the craftsmen were simply taken away from their businesses, the businesses closed by agency fiat, and thus, through an administrative act, the legislation was completely hollowed out.

At the same it became clear that in an economic order that was mainly centrally-planned, businesses and households were perpetually led to seek evasions (purchasing on the black market, bypassing price fixing, and so on). Such evasions altogether undermine the foundations of the rule of law. One smiles at first when one hears from them. But in truth, it is a serious matter that the person who is the most efficient at circumventing the legal order is always the one who fares best. Naturally, in addition to this, came an increase in bribes, which blossomed under such an economic order.

In the end, the rule of law in Germany was undermined mainly by the change in working conditions. Earlier, the private employment contract had developed into the

collective agreement, but then a crossover to central planning of labour occurred. In this way, the sphere of freedom of workers and employees, and of every single German, was very seriously curtailed. At any time, one could be forced to leave his hometown, his family and his workplace. That is when the crossover to bondage and slavery took place. The role of the employment office was no longer just placement, but giving orders with respect to employment. With this, the rule of law completely disintegrates. The individual's sphere of freedom virtually disappears. One can then see that the centrally-planned economy had precisely the opposite effect of what the many workers among their followers had hoped for. It brought in its wake absolute loyalty, the elimination of their sphere of rights and of their freedom. That is an underlying theme in your book. Germany's experience shows how very real this danger is.

5. About the top of page 185, where you write that private enterprise also emerges through the pursuit of power, I would simply like to add that for the German experiences this is a very significant issue. There were two types: first, the industrial leaders, who had previously headed a union or a corporate group and that felt quite at ease as directors of central offices of economic planning. They experienced an expansion of their power in that, for instance, unions then took on a mandatory nature and they could issue public law regulations. The second group was formed by young people, who rightly recognized that they could quickly gain power within the framework of central-planning. This group also proved to be very dangerous. The situation was such that young people in government departments or in other planning agencies, who were barely 30, continuously made decisions concerning huge investments, or shutdowns, or the relocation of workers, and in this way wielded the power that they had sought through political struggle.

The crucial advantage of a competition-based order, namely that power is so fragmented that it no longer has a harmful effect, is a drawback to the extent that for many, this makes a competition-based order less attractive. I feel that by the way in the moment at numerous negotiations.

6. With respect to the relation between democracy, liberalism and socialism, I indeed have reservations concerning Tocqueville's sentence that you quote on page 45. It might not be entirely correct to establish the opposition between democracy and socialism in this way. You outline all that needs to be said on that subject on p.99. To sum up, here is how I

understand it: socialism and democracy are incompatible. Second, socialism and liberalism are incompatible. Yet liberalism and democracy are not identical. There also exists, as you yourself show, democracy without freedom. Consequently, socialism is incompatible with two different things, namely democracy and liberalism.

I should, however, write again in more detail on that subject and particularly tell you of the German experiences.

7. Same thing for chapter 12. I fundamentally agree with the characterization made in this chapter. I would, however, like to add two things.

First, one can say that there was always another movement challenging the one that you characterize as the "Neo-German movement". This movement was made up of the Germans who were and are defined by Goethe, Humboldt, Kant, etc. But alongside, there always were, and still are, men who dissented for decades. There you find a long tradition, from Krauss through Delbrück, and from Mangoldt to Dietzel, and to us, the younger generation. One should however bear in mind that, for example, Moeller van Bruck (with whom, by the way, I have personally had many discussions) or Spengler spoke of liberals with open hatred; liberals who, though they were unorganised, were actually there. Yet it was quite remarkable that in 1941, during a two-day discussion, the speech that I have enclosed here was hardly criticized by either the representatives of the commissioner in charge of prices, of the ministry of economics, of other central agencies and of the *Reichsbank*; in fact, the speech was largely met with approval, and only a few professors of the Historical School disagreed with it. If one wants to sum up the general intellectual situation here, one could perhaps say that in Germany, a classic and a romantic movement developed side by side. Romanticism has changed a lot under the influence of Nietzsche and Naturalism, and with Jünger it is different from what it used to be. It has become massive and violent. But alongside there has always been another movement, which, as I believe, also represents a facet of the German intellectual life, even though in the past few decades, and especially because of National Socialism, it was forced into the catacombs.

About the description of the details, I would like to note that, in my view, the influence of Sombart is perhaps overemphasized. After all, the entire Historical School has already argued along those lines. Of the most recent proponents, Spann may be more important than Plenge, for instance. This massive confrontation between universalism and individualism has had a strong impact on the younger generation. They call themselves

the *Tatkreis* ("Action Circle"). On this topic, Lutz published an excellent article in 1933 in the *Tatwelt*, I am sure you can easily get it from him.

With these words I will conclude. I hope that you receive the version of this letter which contains the documents. About your plans for the coming year, please especially consider a visit here.

With kindest regards,

Yours faithfully.

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