

DISCURSIVE STRATEGIES IN THE KEYNES-HAYEK DEBATE: BUILDING A LIBERAL CRITIQUE

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This article addresses an analysis of discourse based on Michel Foucault's "order of discourse" to comprehend which discursive forces influenced Keynes's mode of thought and his liberal critique. The article returns to the Keynes-Hayek debate to explore the possibilities of considering Hayek as a reverse influence in Keynes's late beliefs on the limits of state action and socially desired ends. An understanding of Keynes's view on the state and economic action requires identifying the underlying strategies of his discourse when criticizing Hayek's spontaneous liberalism. More specifically, Hayek's liberal views promoted a reverse and discontinuous force that contributed to reinforce Keynes's mode of thought.

JEL Classification: B31, B49, B50.

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It is well known that Keynes and Hayek exchanged several letters between 1927 and 1944, besides writing journal articles, newspaper notes, and book reviews, in which each addressed and criticized the other – as well as explicitly defending their own opinions against such challenges (see *inter alia* Ingraio, 2005 and Wapshott, 2011). However, to what extent, and how, these exchanges shaped their respective views on politics, philosophy, and economics still remains a matter of debate. In what follows, this article offers a Foucauldian analysis of discourse to help comprehend how the discursive forces at work in the Keynes-Hayek exchanges shaped Keynes’s critique of Hayek and how, in turn, they might have shaped Keynes’s politics more broadly.

Section 1 briefly outlines the case for a critical discourse analysis based on Foucault’s approach to power and language. Section 2 presents some central points for understanding Keynes’s critique of liberalism and his view about the necessity of governmental action. Hayek’s theory of spontaneous order and state limitation is set out in Section 3. Section 4 then explores certain elements of both Keynes’s political thought and his concrete policy recommendations, in order to demonstrate how Hayek’s interventions played a crucial role in their formation. Specifically, this section focuses on a series of articles and letters written between 1931 and 1944, in which Keynes and Hayek discussed their views on economic dynamics, economic crises, and the role of the state. The final section offers some concluding observations on the construction Keynes’s “middle way” politics – a position which, it has to be said, placed him in a distinctive position at the time.

I. A FOUCAULDIAN APPROACH TO DISCOURSE ANALYSIS

Michel Foucault emphasized how certain conditions limited and/or institutionalized discursive formations, in which discourses can reveal hidden complexities and power relations beyond the spoken/written word. This means that understanding the forces that enabled a specific

discourse to emerge at a certain time and place is as important as analyzing the macro discourse itself. Foucault's methodological prescriptions for investigating a discourse involved four key strategies: reversal, discontinuity, specificity, and exteriority (Foucault, 1971). For him, a detailed analysis of discourse should encompass elements and features beyond the discourse itself – in particular, hidden influences, social contexts, or negative forces.

Firstly, the strategy of *reversal* explores the inverse and negative role of discourses stressing their emergence and their contexts of dominance. A discourse analysis reveals how opposing discourses work as influences in a reverse and discontinuous way by showing how actors strengthen their arguments – sometimes by using the opponent's language or method – to reinforce their own position. This strategy urges us to discard the notion that thought is always essentially rational, positive, and progressive. For Foucault, this principle governs the other three.

Next, Foucault (1991) advocates replacing assumptions of continuity and non-contradiction with a strategy of exploring *discontinuities*, which implies a two-step process. First, it means abandoning continuities – such as preconceived traditions, influences and habits of thought – so as to render other discursive forms possible and visible. Second, it means leaving aside psychological explanations of change – methodological individualism, the genius of great inventions, crises of conscience, and the like – and turning instead to other transformations that constitute, rather than simply provoke, change. Foucault rejects the notion of history as a single-caused homogenous continuum, rather emphasizing the ruptures, breaks, shifts, and mutations in the traditional narrative. This does not mean that one should always assume that discontinuity exists; but rather that we should look at “continuities” with suspicion (1984).

Thirdly, the strategy of *specificity* suggests substituting general forms, abstract elements, and universal effects of discourses for an analysis of transformations in their own

causal explanations and conditions (Foucault, 1991). Accordingly, specificity does not assume prior discourses, or pre-established symbols, that make a statement possible. Instead, it considers a discourse as something specific to its own time and space.

Lastly, Foucault recommends adopting the strategy of *exteriority*, inviting us to reject the idea that we must always try to reach the internal and ultimate meaning of a discourse. On the contrary, meanings can also be found in the surface of discourses. The strategy of exteriority thus aims to consider other conditions of possibility located outside a discourse – such as external facts, forces, actors, and power relations.

Foucault's four discursive strategies allow scholars to explore particular episodes in the history of political economy in a unique way. By understanding how discourses are constituted from economic ideas – and examining how new theories and arguments emerge from criticizing conflicting views – it may be possible to reach a more comprehensive account of how the character and content of Keynes's politics emerged in his encounters with Hayek.

II. KEYNES'S "POLITICS" AND A CRITIQUE OF ECONOMIC LIBERALISM

An analysis of Keynes's political view also requires an understanding of his reflections about modes of production – free-market capitalism and the centrally-planned economy –, as well as their embedded ideologies – liberalism and socialism. Keynes's biographer Robert Skidelsky (2003) stresses that as an undergraduate Keynes was not as much as interested in politics as he was in philosophy and formal logic; his interests changed drastically, however, after the First World War. In *Essays in Persuasion*, Keynes dedicated himself to the discussion of several political issues during the late 1920s and early 1930s, particularly the conflicts between liberalism and socialism. Of particular interest was Keynes's own critique to socialism, which, for him, had lost its capacity to deal with real problems due to its ideological dependence (CW IX, 2013a).

Keynes did not oppose socialism and liberalism completely. He claimed that both socialism and liberalism stemmed from the same historical and theoretical origins by either accepting or denying the utilitarian character founded in Benthamian principles. Or, put differently, they shared similar “conditions of possibility” (Foucault, 1989) by indicating that both socialism and liberalism shared some fundamental characteristics regarding their ontology and epistemology. This sheds light on how Keynes’s and Hayek’s discourses understood each one of these two modes of production (and ideologies), and how they built their theories around them.

Keynes was indeed a liberal, but not in the strict economic sense of the term. He believed in the liberal view of doing politics and had an open mind to many social issues. However, he criticized economic liberalism and its assumption regarding a complete rejection of state intervention, especially in times of economic crises. Keynes addressed a direct critique to *laissez-faire* liberalism and to Russian communism in four of his *Essays in Persuasion* (CW IX, 2013a), which constituted a separate section entitled “Politics”: *A Short View of Russia* [1925]; *The End of Laissez-Faire* [1926]; *Am I a Liberal?* [1925]; and *Liberalism and Labour* [1926].

In the second essay¹ (1926), Keynes investigated the origins and metaphysical foundations of the idea of *laissez-faire* liberalism, which he attributed to a combination between the ideas of “natural liberty” of economic activities and “enlightened” self-interest in the 18th and 19th century. For Keynes, the ideas of self-interest and natural liberty suited conservative politicians and lawyers conveniently, as they provided an intellectual foundation to the rights of property and to the liberty of individuals to act freely. In Keynes’s view (1926), this was the reason why liberal ideas became so popular and effective in the 18th and 19th centuries.

Historically, *laissez-faire* and individualism emerged as a suitable ideology in late 19th century. Keynes (1926) emphasizes how 18th century governments were corrupt and incompetent, stressing that from 1750 to 1850 material progress came largely from individual initiative and private enterprises, which endorsed individualism and *laissez-faire* as an acceptable philosophy for business-driven, conservative men. When discussing economic thought, however, Keynes deconstructed some of the myths about associating British classical political economy with market deregulation². Quoting Keynes (1926, p. 4): “The phrase of *laissez-faire* is not to be found in the works of Adam Smith, of Ricardo, or of Malthus. Even the idea is not present in a dogmatic form in any of these authors.” Actually, aside from French physiocrats such as Pierre-Paul Le Mercier de La Rivière and François Quesnay, only Jeremy Bentham mentioned the idea of *laissez-faire* in his late writings but reframing it from a utilitarian perspective that reconceived social and economic life in an intense way, as to be understood with the principles of *laissez-faire* (Keynes, 1926).

Economists played an active role in spreading the notion of *laissez-faire* to the public arena in the late 19th century, demonstrating a narrow connection between the theoretical field of ideas and the public, practical sphere of public policies. Keynes (1926) mentions two ideological assumptions that transcended from the ideological context of *laissez-faire* to the practical world of norms and rules. Firstly, that individualism and self-interest led to a social selection norm that there must be no mercy or protection for those who were bankrupt or less efficient. Secondly, how *laissez-faire* led to the institutionalization of the love for money in the sense that liberalism created a necessity for unlimited private money-making and enabled a system that put first those skilful or fortunate individuals. Keynes’s criticisms to *laissez-faire* liberalism draw from John Stuart Mill’s tradition of moral philosophy (Baldwin, 2006; Mattos, 2015), which rejected the acquisitive values of capitalism, as well as its ability to solve the problems of distribution of wealth and poverty spontaneously.

Keynes criticized this individualistic capitalism. In his essay *Am I a Liberal?* (CW IX, 2013a) [1925], he stresses his concerns with a liberal program not in the historic sense of the analysis, but how it affects current political and economic issues pragmatically. Interestingly, Keynes returned to Bentham's nomenclature of a political *Agenda* (Bentham, 1843) to describe where the state should and should not interfere³. Keynes advocated that the ideal size for the unit of control and organization is somewhere in between the individual and the state: on semi-autonomous bodies within the state that use the criteria of public good as their guide of action, such as universities or Central Banks. In this sense, Keynes's "middle way" proposal did not exclude the individual nor the institution of the state (Keynes, CW IX, 2013a).

Keynes's view about the world offered both a "new way" and a "middle way". The "new way" refers to his macroeconomic theory, which identified the problems in an insufficient aggregate demand to solve the 1929 economic crisis. The "middle way" represented his political view that deviated from both Marxism and Liberalism, in which Keynes proposed a social philosophy that would be a compromise between capital and labour, thus rejecting socialist forms of planned control, liberal *laissez-faire* and individualism. Keynes's philosophical thought thus influenced his policy proposals in two possible ways: the need for rules in policy-making under uncertainty; and the ethical purpose of politics.

Firstly, Keynes defended that in face of risk and uncertainty, governments should act to promote social contentment that not only involve political and economic tools, but broader social actions including the expansion of schools and universities, leisure centres for the population and support for the arts. Under uncertainty a *laissez-faire* market system cannot ensure an effective level of aggregate demand that makes profitable for firms to employ capital and labour fully (Robinson, 1956). In this case it is unlikely that, in the absence of active government policy, full employment can be achieved. Hence governments should act as a guide to economic activity both directly and indirectly: directly in the sense that governments can

actually act as an economic entity that hires employees and controls capital flows via fiscal policies and investments; and indirectly in the sense that the state may affect economic reality via monetary policy, interest rates, taxes and international trade that result in incentives to production and employment (Keynes, *CW XX*, 2013b).

Secondly, for Keynes politics represented a form of practical ethics. Indeed, Keynes's politics did not rule out ethics; on the contrary, politics was a branch of practical ethics insofar as it was the science of how governments should act and behave (Skidelsky, 2010). Noteworthy is that Keynes also offered an ethical critique of liberalism by rejecting the ideology of private money-making and the love of money (Andrews, 2010). Both politics and economics represented practical means of action to achieve the ethical end of good life; it was the government's duty to facilitate the pursuit of such goods by members of the community.

Conceptualizing Keynes's arguments from a reverse perspective reinforces the strength and persuasion of his arguments, especially in his critique of liberalism. The reverse strategy of a discourse sheds light on the Keynes-Hayek debate inasmuch as we can comprehend Keynes's arguments about the need of state intervention in economics from a clear, critical point of view in his rejoinders to Hayek. The next section introduces Hayek's liberal arguments and his defence of a spontaneous order, followed by a discourse analysis of their intellectual debate.

III. HAYEK'S INDIVIDUALISM AND SPONTANEOUS ORDER

Friedrich Hayek was a major influence for 20th century liberal economic thought, especially for the Austrian school of economics, as well as being linked to German ordoliberalism and American neoliberalism. He had a founding role in neoliberal think-tanks, such as the Walter Lippmann Colloquium in 1938, the Institute for Economic Affairs (IEA) in 1945, and the Mont Pèlerin Society in 1947. Additionally, he was a key influence on early neoliberal thought in the

United Kingdom as a lecturer of the London School of Economics and in the United States as a member of the University of Chicago.

Hayek developed a unique economic theory by dealing with two domains of expertise, business cycles and social and political philosophy, whilst rejecting some neoclassical conceptions regarding knowledge, assumptions and principles, such as equilibrium and *homo economicus*. Hayek's famous *The Road to Serfdom* (2001) [1944] analyses the possibilities and risks of emerging totalitarian regimes from government control and centralized decision-making, particularly because it suppresses the individual and its intrinsic freedom. He directed his critique to totalitarian regimes, such as communism, and to intervener modes of governance, such as Keynesian economic and social policies.

Some scholars claim that Hayek did not defend the exclusion or the rejection of state action, but rather addressed a fundamental shift on the role of the state in the economy and in civil society (Skidelsky, 2006; Mirowski and Plehwe, 2009). He saw the need of the state for multiple purposes, including an active provision and enforcement of a legal framework to ensure that the mechanism of market competition functions well. Put differently, Hayek was not favouring the elimination of the state per se, but a fundamental restriction on its role to be limited to the "Rule of Law", which is different than the principle of *laissez-faire*. It is not about freeing the market forces and allowing them to act freely through a rejection of the institution of the state in the economy, but to actively pursue the implementation of the mechanism of prices, individual freedom and competitive markets in the economy (see for instance Statement of Aims – Mont Pèlerin Society, 1947).

The conception of Hayekian liberalism was a response to socialism and centralized forms of government, mainly because socialism is incompatible with individual freedom, which is a central feature for Hayek's theory (Kukathas, 2006). True individualism, for Hayek (1948), emerged with John Locke, Bernard Mandeville and David Hume, and it was later

improved by Adam Smith and Edmund Burke. Hayek considers individualism a theory of society in which one presupposes the individual as the first ontological instance to understand the social processes⁴. With individualism also comes a limitation for coercive and interventionist powers, thus representing the Hayekian solution to avoid totalitarian powers in the sense that the state should only interfere through the principle of law. Therefore, Hayek's two main political principles that involve state action were based on spontaneous order and the Rule of Law.

First, Hayek considered the principle of spontaneous order as the basis for his libertarian system. For him (1982), one can conceive the notion of "order" in two different senses: as an authoritarian, artificial, exogenously created system; or as a free, self-generating, endogenous force, such as the market force. Actually, he compared the latter form of order to a biological system that emerged from natural forces: "[a]ll that is necessary to preserve such an abstract order is that a certain structure of relationships be maintained, or that elements of a certain kind [...] continue to be related in a certain manner." (Hayek, 1982, p. 39). Therefore, spontaneous order is a product of forces or systems that interact (such as human forces) but are not created from a pre-calculated and intended design.

Given that an order emerges spontaneously, institutions should not change its nature. This is why Hayek believed that society should rely on the principle of spontaneous order to limit the powers to control: those forms of control are artificially created (by society), which are not as effective as those institutions that emerge spontaneously. Hence in social contexts the economic order of the market would suit the arrangements and organization of public action better than an "artificial" governmental action over the economy. Hayek (1990) emphasized the role of the state and other formal institutions in freeing the system, such as assuring that the market competition system has its necessary conditions to function well.

Although Hayek (1948) was against the neoclassical premises of perfect competition theory and competitive equilibrium⁵, he believed that competition is a natural force of the market, and therefore it should not be suppressed. Hayek's thoughts about competition start from the context of individual behaviour, which emphasized Hayek's methodological individualism. He adopted a metaphor of the enterprise to understand how decisions and actions of economic agents are undertaken in reality (Hayek, 1948), in which the entrepreneur is the driving force of the market process that ensures the good functioning of the economy.

Secondly, Hayek (1990) links the spontaneous order of the market to "rules of law".⁶ Given his theory of how that specific order emerges – it is not the result of a "miracle", but a combination of unintended rules of conduct that constituted a system of repeated activities – the rules created with the aim of regulating the market order should actually improve and maintain the order, without annulling its influences and forces.

In *The Road to Serfdom* (2001) Hayek claims that the Rule of Law is what distinguishes free countries from totalitarian regimes. If a state only governs through the instrument of law, it avoids arbitrary decisions from statesmen and certain groups of power. In the case of the economy, governments should fix the laws that determine the conditions under which the available resources may be used, leaving to the individuals the decision for what ends they are to be used. Accordingly, economic planning should be avoided because it is unable to provide as many desired results as a free economy.

One can then define Hayek's conception of governmental action as a recommendation that does not exclude the state, but imposes some rules of action. For Hayek, keeping the state from acting coercively does not restrain it from providing some services and designing laws for individuals under certain conditions, such as supplying services that otherwise would not be supplied at all. In that sense, Hayek (1990 and 2011) establishes an agenda that defines three principles in which government services are compatible with his liberal principles, as long as:

(1) the government does not claim a monopoly for providing services, such as social insurance, and/or does not restrain the market to provide them; (2) the means are raised by taxation on uniform principles, and taxation is not used as an instrument for the distribution of income; and (3) the wants satisfied are collective wants of the community as a whole and not merely wants of particular groups of interest.

Hayek's state agenda excluded the possibility of governments creating monopolies or other means that could interfere in markets or economic competition. Moreover, it disregarded the use of public means to promote income distribution and to promote group interests that did not coincide with collective interest. The state must not interfere in the economic agenda (inequality, earnings, prices, consumption patterns) as a means to achieve social ends. In this case, the state should only interfere through legal-formal terms, thus defining a framework within which economic agents can make their own decisions freely.

In the *Road to Serfdom*, Hayek's famously addressed a critique to the welfare state model and welfare policies in general, claiming these would lead to socialist modes of governance as they would require economic planning – which would represent a risk for implementing a regime of nationalization of the means of production –. In his later works (2011), Hayek confirmed his view about the dangers of transforming the welfare state into a coercive and controlling system that restricts human liberties.

The ideological and theoretical differences between Hayek and Keynes about involving politics and economic policies are indeed striking, despite their shared epistemological position about the nature and effects of uncertainty (Skidelsky, 2010). Their intellectual debate deserves a separate investigation based on a discursive perspective, underpinning their arguments and rejoinders about the limits of state action.

IV. A DISCOURSE ANALYSIS OF KEYNES'S REPLY TO HAYEK: STRATEGIES OF THOUGHT AND THE BUILDING OF A STATE THEORY

What were the main arguments adopted by Keynes in his reply to Hayek's critique? How can they be analysed in the light of discursive formations and ruptures, particularly their ideas about the limits of state action? How did they contribute to build Keynes's liberal critique?

The intellectual clash between Keynes and Hayek has dominated several academic and non-academic publications (see *inter alia* Steele, 2001; Wapshott, 2011), particularly after the global financial crisis of 2007-8 when Keynesianism re-emerged as an alternative to neoliberalism and the ideal of market superiority. Keynes's and Hayek's views about the state and their prescriptions about economic policies became increasingly popular, reviving the debate regarding the limits of state action, power relations, public participation in the economy and individual liberty. Even though some discrepancies between them have been suggested elsewhere (Carabelli and De Vecchi, 1999), a discursive and linguistic investigation into their debate has not been yet provided by historians of political economy.

A discourse analysis of their arguments and rhetoric means exploring the performativity of the discourse beyond the spoken/written word. The Foucauldian approach suggests that a discourse can be comprised of negative and reverse influences because it rejects previously consolidated ideas that reflect certain modes of thinking, social practices and power relations. Then, discourses can also create the necessary conditions of possibility for new ideas, theories and critiques to exist. One must then look into the external elements, social contexts and negative influences of a discourse to understand its complexity and meaning – it often reveals hidden elements such as pre-conceived notions, assumptions, backgrounds, power relations and criticisms that indicate how a discourse was built.

A reassessment of Keynes and Hayek's arguments requires a critical reading of their original letters and essays in the light of their ideological backgrounds. The way Keynes built

his arguments in his replies to Hayek helped him to shape and strengthen his own theory by using “reverse” and “discontinuous” discursive strategies. As their controversy was not only about the political interventions of the state, but also about other issues that involved the dynamics of economic foundations (such as the role of money and monetary policy, inflation, interest rates and investment levels), and the nature of economic crises, this article explores each of their arguments in the light of a discursive structure.

The correspondence between Keynes and Hayek can be divided in three distinct moments: (i) 1927-1929, composed by essays of mutual biographical interest; (ii) 1931-1932, including their theoretical observations and critiques in private letters and public notes; and (iii) 1933-1944, including broader discussions such as social contacts and academic affairs (Ingrao, 2005). This article focuses on the last two moments (1931-1944), addressing some excerpts from letters, articles and newspaper comments. This includes their public letter exchange in *The Times* in October, 1932⁷; Hayek’s review of Keynes’s *Treatise on Money* in 1931, and the following rejoinders (Hayek, 1931 and Keynes, 1931); and a private letter in which Keynes commented on Hayek’s *The Road to Serfdom* in 1944 (in Wapshott, 2011).

Keynes confronted Hayek on three main issues: (1) how economic principles function in reality; (2) the extent of governmental action to solve economic problems; and (3) the ethical limits of state conduct towards the individual and/or the collective. These arguments illustrate a refinement and a delimitation of Keynes’s discourse in reply to Hayek, which characterized a “reverse influence” to Keynesian theory.

Economic principles and dynamics

Although Keynes and Hayek diverged in many theoretical aspects, they were immersed in the same historical-epistemic moment, which affected the development of their arguments and theories. Our conceptual review (sections 2 and 3) suggest how both intellectuals had different

epistemological perspectives about the existence of uncertainty in reality, particularly in the economy. Whereas Hayek was concerned about governmental uncertainty – and its incapacity to know exactly what society needs – Keynes focused on the harmful economic effects of uncertainty, and how governments should act as a collective leader that should take precautions against it. The perception of the notion of “uncertainty” as related to knowledge is crucial in their debate. Hayek understood that relevant knowledge is dispersed and available among decision-makers, but that, while scattered, is complete (market prices concentrate this dispersed knowledge into a form that alert knowledgeable entrepreneurs) (Brady, 2011). Keynes, however, considered “uncertainty” as a fundamental and inevitable social element, meaning that while full knowledge is not possible, coordinated governmental action can attenuate it.

This connection between their ontological foundations and the nature and dynamics of economic reality deserves further attention. In an article published in *Economica* (August 1931), Hayek demonstrated his beliefs in business cycles as the most consistent theory for describing economic reality. For him, understanding the cycles demanded an “equilibrium theory” perspective in which economic dynamics would work from a self-adjusting process in the forces of supply and demand in a free market until they are equalized. Hayek (1931) often referred to Keynes’s *Treatise on Money* and its approach to non-neutral money. Hayek saw money as a limited element in the economy in the sense of supporting a neutral and stable money supply (thereby a limited monetary policy and gold standard), emphasizing other elements such as prices and interest rates (Hayek, 1967), mainly influenced by Knut Wicksell.

Both central banks and household consumption decisions can affect the cycle. An increase on household savings for future consumption lowers the interest rates in the present and pushes credit up, probably led by a change in intertemporal consumption plans. This causes an increase in credit supply, inducing firms to borrow with lower interest rates. With that newly created purchasing power, firms begin to lengthen their processes of production by taking into

account only the future levels of consumption, forcing consumers to reduce their real desired consumption level at the present. This unmet demand for current consumption goods pushes the prices up, leading to higher market interest rates (Hayek, 1967).

Similarly, if central banks inject newly created money in the economy, banks expand credit and cause a lowering in the market interest rate. However, in this case there is not an actual change in time preferences. When banks expand credit they induce higher levels of spending in the present, such as consumption, investments and loans, which leads to an unbalance between savings and investment and to a boom in the economy. Hayek's (1967) solution is a "neutral" monetary policy that equals savings and investment levels again through an increase on the interest rates, not money expansion. Interestingly, Hayek criticizes Keynes's integrated approach to investment: "(...) his whole concept of investment is ambiguous, and that its meaning is constantly shifting between the idea of any surplus beyond the reproduction of the identical capital goods which have been used up in current production and the idea of any addition to the total value of the capital goods, renders it still less adequate to account for that phenomenon" (Hayek, 1931, p. 274).

Keynes disagreed from Hayek's conception of economic reality and the ways economic variables fluctuated. Keynes addressed a monetary theory of production in which money represents a non-neutral asset that influences individual and collective economic decisions and liquidity preferences. He saw a prominent role of non-economic elements and their possible effects in the economy, such as expectations, ontological uncertainty, social conventions and the role of confidence.

Keynes's rejoinder to Hayek in *Economica* (November 1931) demonstrates a clarification of what he meant by savings and investment, and how these two entities are integrated in such a way in the economy that their exchanges by one or the other do not affect the total amount available in the banking system. "Dr. Hayek concludes", Keynes says, "that

the necessary condition of avoiding Credit Cycles is for the banking system to maintain the effective quantity of money absolutely and forever unaltered.” “My analysis is quite different from this”, Keynes stresses, “saving and investment (as I define them) can get out of gear without any change on the part of the banking system from ‘neutrality’ as defined by Dr. Hayek, (...) there being no automatic mechanism in the economic system” (1931, p. 393).

The Keynesian proposal for understanding economic dynamics represents an abandonment of certain continuities and preconceived traditions, such as the idea of neutral money (and economic neutrality in general), economic equilibrium whilst acknowledging the importance of non-economic influences (psychology, expectations), thereby designing a new form of economic discourse. Insofar as Keynes sought to criticize classical economic foundations, his rhetoric involved the “reverse” (“discontinuous”, “specific” and “exterior”) discursive strategy to build his own theory. Additionally, although inspired by preconceived discourses or pre-established ideas about economic dynamics and reality as a whole, he addressed his own view based on other traditions and exploring previously ignored elements in economic theory. His arguments in the debate with Hayek makes his strategy of reversal even more explicit.

Economic crises and governmental action

The 1929 crash also illustrates Hayek’s and Keynes’s views of economic issues and the role of the state. Due to their different backgrounds and “temperaments” (Skidelsky, 2006), however, they presented opposite theoretical and policy responses of how to solve the crisis, besides conceiving economic agents and institutions differently. Hayek believed that low interest rates caused low savings level and overinvestment in securities and real estate, leading to a boom and later to a bust. Keynes, however, attributed the crisis to negative expectations of future profits from investors, leading to low levels of consumption and underinvestment. If a fall in

consumption appears to be long-term, businessmen will lower their expectations to invest and to hire, causing an aggregate demand crisis.

Whereas Keynes argued that interest rate policy and public works expenditure (and at one stage even tariffs to protect industry) could be used to alleviate depression and to promote recovery, Hayek considered these precisely the opposite of what was required. For Hayek they would only serve to prolong an expansion that was unsustainable and was bound, eventually, to collapse. To follow such a course would not just postpone something that was inevitable: the longer the maladjustment continued, the worse would be the ensuing crisis.

Hayek's strongest criticisms of Keynes's theory included the attempts to stimulate the economy through injections of money; and active governmental intervention, which would only prolong the crisis. Additionally, fomenting consumption demand would also be ineffective as a solution to the crisis. Inasmuch consumption was an intrinsic characteristic of Hayek's business cycle, it should not be artificially stimulated through temporary policies.

In their letter exchange for *The Times* (October 1932), they diverged about the motives of economic activity; more specifically, the role of spending, savings and private investments in that troubled economic scenario. Hayek's (and his LSE colleagues) first comment on October 10th defended a rise in savings and the relevance of private investments as the solution for the crisis, which indicated a direct defence for liberalizing policies that involved free trade, fluctuating prices and private investments.

In Keynes's (and his Cambridge and Oxford associates) rejoinder on October 17th (published as Macgregor et al., 1932), they stressed the potential dangers of an increase in savings level, particularly because savings tend not to be spent on production or consumption goods during a recessive context, emphasizing the role of consumption for overall aggregate demand. Keynes says: "(...) when a man economizes in consumption, and lets the fruit of his economy pile up in bank balances or even in the purchase of existing securities, the released

real resources do not find new home waiting for them” (Macgregor et al., 1932, p. 13). For Keynes, a pessimistic economic scenario blocks new entries of investments, which is intensified by the private economy.

Keynes’s rejoining comment derives from his distinction between savings and investment due to their ontological magnitude and secondary economic impacts (albeit they are equal in amount, their nature and economic impacts are different). Again, he resorted to a reverse discursive strategy to abandon the preconceived notion that savings is equal to investment, at the same time he provides an exteriority argument beyond the theoretical discussion, using practical policies to reinforce his point. He says: “(...) in present conditions, private economy does not transfer from consumption to investment part of an unchanged national real income. On the contrary, it cuts down the national income” (Macgregor et al., 1932, p. 13).

Keynes also sheds light on the role of adequate practical economic policies when underpinning the problems of encouraging private investments without adequate policies. In this case, an economic downturn would reduce private investments due to lack of confidence and pessimistic expectations, therefore resulting in no real stimulus for the economy to recover. The reverse approach to Hayek’s proposal demonstrates the performativity of the practical argument when associated to fundamental theoretical differences in each world view.

It is then possible to investigate how each intellectual conceived the existence and the role of the state as a policy-maker from their own world views, political proposals and possible answers to the crisis. Hayek did not reject the existence or the legitimacy of governmental intervention. Nevertheless, given his ontological understanding of the state and society from a liberal perspective, Hayek considered the state not as an active economic subject, but as rule-maker that contributes indirectly to economic actions. In Hayek’s final rejoinder to Keynes’s letter on October 19th (published as Gregory et al., 1932) he says:

If the Government wish to help revival, the right way for them to proceed is, not to revert to their old habits of lavish expenditure, but to abolish those restrictions on trade and the free movement of capital (including restrictions on new issues) which are at present impeding even the beginning of recovery. (Gregory et al., 1932, p. 10).

Hayek believed in the role of private investments as the way to get out of the crisis: “We, on the contrary, believe that one of the main difficulties of the world to-day [sic] is a deficiency of investment – a depression of the industries making for capital extension, rather than of the industries making directly for consumption.” (Gregory et al., 1932). Together with stimulating private investments, Hayek and his LSE associates suggested a formal role of the state in the sense of creating and imposing rules and conditions to stimulate those private investments, rather than being economically active and actively increasing public expenditure. Indeed, Hayek’s view also becomes more refined and presents a clear political recommendation during this letter exchange.

Two years before, in 1930, Keynes presented his economic policies in an attempt to mitigate the effects of the crisis. In his essay *The Great Slump of 1930* (Keynes, CWIX, 2013a), as well as in several of his letters to British statesmen and public radio broadcasts (Keynes, CWXX, 2013b), he discussed unemployment and social policies, industrial incentives, international financial assistance and foreign trade. For Keynes, the biggest issue of that moment was the lack of investment and enterprise at home, together with an expansion of investments abroad, leading to a loss of gold, higher interest rates and credit reduction.

Consequently, this discouraged investment and enterprise at home, causing unemployment and low profits. As a solution, in his 1930 BBC radio broadcast Keynes says he had been “in favour for a good long time of a large programme of capital expenditure at

home that would employ men and would give an outlet for our savings without putting pressure on the gold reserves of the Bank of England” (CW XX, 2013b).

Keynes’s plan required direct state guidance in controlling public spending and reorganizing expectations and confidence. This reflected the performativity of Keynes’s ethical-philosophical view towards his economic recommendations: his mode of thought emphasized the role of the state as an entity that could change the future of society as a collective, organic entity. In his writings about solving economic issues, Keynes seemed to address a reverse principle (or strategy) when defending the normative role of the state, also emphasizing other elements of the economy, such as uncertainty and expectations.

If Keynes managed to associate his own mode of thought and ontological principles to practical argumentative strategies about the role of the state, his discourse emanated a specific socio-historical background associated to a certain view of the world. As mentioned earlier in this article, if a discourse exercises certain patterns, norms and causal powers, Keynes’s case illustrates how the negative, or “reverse” argument against Hayek’s liberal view can also work as a rhetorical strategy to constitute and reinforce his own theory about state action.

Ethical limits for State conduct

Even though both intellectuals had strong philosophical backgrounds in similar historical periods, their discursive strategies and arguments towards the concepts of “liberalism”, “ethics” and “individual” are distinct. If their discourses reveal their ontological views of reality and how economics is placed therein, a reply to each of their comments tries to deconstruct and re-elaborate their initial assumptions, which is Keynes’s case when he addresses a reverse strategy to Hayek’s arguments.

Hayek’s theory of liberty was bounded by the law, and his justification of liberty was instrumental: the central planner has less knowledge than exists, hence the market forces work

as a better guide to individuals in the sense of an “entrepreneur of the self” than state-driven or social-driven forces. Individuals consider the impersonal market signals in their decision process within a legal framework to decide about economic and non-economic aspects of life that will result in relative remunerations (Hayek, 1948). Then, the institution of the state is left out of the decision-making process, which is now guided by the market.

Hayek feared the gradual encroachments of the welfare state in the economy and society, especially under the argument of social justice as a justification for interventions in the economy. Under the Hayekian logic, those arguments favouring social justice and income distribution may actually reflect the interests of some groups, and not the society as a whole. In this sense, welfare policies could present adverse results that sometimes do not promote real, collective welfare for all social spheres.

Keynes, on the contrary, demonstrated a more pragmatic approach as he considered ethics and the power of ideas as the great persuasive forces for practical governmental action. He did not seek to understand the formal means of the state legally and politically speaking, but he focused on real economic and political concerns of a historical period in which the state had a crucial role for promoting economic and social solutions, hence an *end-state liberal* (Peacock, 1993).

A letter from Keynes to Hayek in April 4th, 1944⁸ reveals that Keynes commented Hayek’s recently published piece *The Road to Serfdom*. Keynes defended a middle-way of ideas and governmental action by criticizing Hayek’s theory that socialism and other planned modes of production might lead to totalitarianism. Keynes stresses:

[W]hat we want is not no planning, [...] [b]ut the planning should take place in a community in which as many people as possible, both leaders and followers, wholly share your moral position. Moderate planning will be safe if those carrying it out are rightly orientated in their own minds and hearts to the moral issue.

[...] What we need is the restoration of right moral thinking – a return to proper moral values in our social philosophy. (Keynes, *CW XXVII*, 2013c, p. 387).

In his letter to Hayek, Keynes advocated a moderate governmental planning of domestic activities, particularly those that involve economic and social issues based on an ethical conduct.

Keynes also believed in public-spirited people that worked for the collective good, emphasizing the social role of public action. Indeed, for Keynes ethics could not be separated from practical political and economic activities, such as policy-making, and he makes this point clear when elaborating a discourse to criticize Hayek. Unlike Hayek's libertarian arguments that rejects planning or other forms of active economic and social policy under the threatening concern of totalitarianism, Keynes relied on a democratic form of pragmatic capitalism: society demands a coordinated action of institutions that have that specific end of social contentment.

Keynes's interest in fostering the development of a persuasive public-spiritedness in economic life, which overcame a traditional political expansion of the state. We can see that when he advocated that self-autonomous bodies should be encouraged by state action, he also included the social role of universities, leisure centres and the arts (Keynes, *CW XXVII*, 2013c), reaching a point where he also considered sex, population and drug issues as a relevant agenda (Keynes, *CW IX*, 2013a).

Keynes's ethical-political view incorporated ontological uncertainty, holism and ethics within traditional aspects of liberal politics, thus conceiving both society and individuals as two mutual-influencing entities. Despite the fact that Keynes did not put all efforts into the forces of the market or into the representative agent (individual), he combined a moderate state intervention in the economy and society with a sense of public ethics that did not annul the individual, indicating clearer and more refined notions in his rejoinders to Hayek.

Understanding the elaboration and strength of Keynes's arguments cannot be fully achieved without going through Hayek's criticism. Indeed, in the light of some of Hayek's observations, Keynes addressed stronger notions and presented clear arguments that accounted for a rejection of the liberal-utilitarian view. Even though Keynes did not pursue a formal theory of the state, one can comprehend some of his delimitations from his philosophical reflections and normative political recommendations of how the state *should* act against Hayek's theory. Once Keynes's arguments clearly defined his rationale towards state action – and how his view differed from the Hayekian approach – one can consider Hayek as a possible reverse influence to Keynes's thoughts.

V. CONCLUDING REMARKS

A discourse analysis of Keynes's and Hayek's thoughts offers some new insights to historians of political economy regarding their rhetoric and argumentative strategies. Both intellectuals diverged about procedural economic means, which originated from their different point views concerning economic reality, institutions and agents. Indeed, they were both liberals and had different conceptions of economics, which derived from their previous philosophical trainings. Nonetheless, both believed in the power of ideas, only diverging on practical terms on how to achieve their intended goals.

A closer look into Keynes's and Hayek's debate in the light of a Foucauldian reading demonstrated two crucial aspects. First, a discontinuous and specific influence of Hayek on Keynes's late beliefs in the sense of going beyond the traditional discourses and schools of thought that influenced the construction of Keynes's theory, such as Malthusian and Marshallian economics. Secondly, an analysis of the communication between Keynes and Hayek indicates a reverse influence inasmuch as Hayek exercised an opposite force to Keynesian thought. Keynes had to deal with Hayek's criticism and create a stronger and more

consistent theory that would account for Hayek's observations by rejecting the Hayekian view, which worked as a reverse influence.

Keynes's debate with Hayek offers a clarification of the Keynesian view of the role of the state and economic agents. It is not that Keynes had not considered and built his beliefs beforehand, but there were some strategies that underlay his discourse and the construction of his arguments in the debate may have played a fundamental role in his thinking. The application of Foucault's principles for discursive analysis was an attempt to bring Keynes's mode of thought into light. Opposing discourses can also work as influences in the reverse and discontinuous sense of the word: intellectuals must strengthen their discourses – sometimes using the opponent's language or method (or strategies) to reinforce their own argument.

¹ Keynes's *Essays in Persuasion* (CW IX, 2013a) [1931] published a different (and shorter) version of *The End of Laissez-Faire*, which excluded the three first sections of the original version of the pamphlet, published by Hogarth Press in July 1926.

² Though many consider Keynes as a Marshallian, particularly on the issue of formal language, one cannot ignore the influences of the 18th and 19th century classical political economy in his ideas. Some Post-Keynesians consider Keynes an old-fashioned classical intellectual in some sense – in the sense of classical political economy's terms –, insisting that he also gave special attention to the issue of labor as a crucial variable in his works (Kregel, 2013).

³ According to Bentham's *agenda*, he defines it: "What the legislator and the minister of the interior have it in their power to do towards increase either of wealth or population, is as nothing in comparison with what is done of course, and without thinking of it, by the judge, and his assistant the minister of police. The cases in which, and the measures by which, the common end may be promoted by the hands of government, may be termed *agenda*. With the view of causing an increase to take place in the mass of national wealth, or with a view to increase of the means either of subsistence or enjoyment, without some special reason, the general rule is, that nothing ought to be done or attempted by government. The motto, or watchword of government, on these occasions, ought to be—Be quiet". (Bentham, 1843, original highlights).

⁴ Hayek's clear distinction of what he considers "true individualism" from other individualistic approaches. The first arose with the British tradition of Locke, Hume, Smith and Burke; whereas the latter emerged from Descartes and the French tradition (Hayek, 1948).

⁵ There is, however, some controversy on the extent Hayek agreed or not with these principles (Eatwell and Milgate, 1994).

⁶ Rule of Law means the rules of the game, or the fixed rules that are announced beforehand that enable individuals to foresee the actions of the government. For Hayek, a liberal society demands the Rule of Law and justice to delimit the scope of individual freedom. Or, following Kukathas (2006, p. 185): "liberalism upholds the idea of a free society in which individual conduct is regulated by rules of justice so that each may pursue his own ends or purposes in peace".

⁷ Original scan retrieved from: http://austrianeconomists.typepad.com/files/cambridge_vs_lse_1932.pdf (accessed 5 November 2018).

⁸ This letter is available for consultation in the archives of LSE (Wapshott, 2011, p. 325, ft. 44), as well as published in Keynes's *Collected Writings* (CW XXVII, 2013c).

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