

Hayek=s Slippery Slope Is There a Third Way?

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The interest in Friedrich Hayek=s famous book, *The Road to Serfdom* (Hayek, 1944), written in the early 1940=s has waxed and waned over the intervening years. Recently, however, there has been a decided renaissance of interest in the book. This interest is by no means confined to this country and to Western Europe but has manifested itself in countries as diverse as China and Russia. There is still controversy, however, both over the message of *Serfdom* and its applicability to current events.

Many critics have charged that the message of *Serfdom* was that totalitarianism would be the inevitable consequence of interferences into the market system. Hayek, later, denied this and responded that the argument of the book was that unless we mend the principles of our policy some very unpleasant consequences will follow, which most of those who advocate those policies do not want. The unpleasant consequences of which Hayek speaks came under the heading of socialism. Hayek originally railed against the socialism that he encountered in his native Austria and in Western Europe. This was, more or less, classical socialism, wherein the state owned the means of production and allocated the resources according to the dictate of bureaucratic officials. The arbitrariness of this procedure was obscured or masked by the notion that this allocation took place according to a plan. Bureaucratic officials, of course, formulated the Aplan.@ In later writings Hayek reformulated the definition of socialism, arguing that socialism has come to mean the extensive redistribution of incomes through taxation, and in the institution of

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the welfare state. Milton Friedman strongly supported this characterization in his adulatory preface to the 1976 reprinting of *Serfdom*.

Hayek had expanded on the ideas of *Serfdom* in a monumental follow-up volume: *The Constitution of Liberty* (Hayek, 1960), followed, in turn by extensions of his thinking in three paperback volumes, (Hayek 1973), (Hayek, 1976) and (Hayek, 1979). In these books Hayek builds a powerful case against the central direction of human activity and argues that economic freedom is not separable from other freedoms. Hayek=s principal argument was that the central direction of economic activity depends on the notion that there is perfect knowledge regarding production and consumption decisions. Were this the case, central planners could assure the economically efficient use of resources. Such perfection of knowledge is not possible however. There will always remain events that are unforeseen and unpredictable, of which no Aplan@ could possibly take cognizance. Hayek argues that the liberty of the individual is essential to leave room for the unforeseen and the unpredictable. He argues, further, that leaving individuals free to pursue their own ends will enable society to make use of far more knowledge than the mind of the wisest despot could devise. (The wisest despot could equate, easily, with the wisest bureaucrat.)

A critic of Hayek, McInnes, concedes the correctness of this argument. Indeed, he summarizes this point nicely, when he notes that the market is the only place where all relevant information becomes available, revealing in price mismatches and anomaly opportunities for entrepreneurs. He agrees with Hayek that the possibility of central control and direction vanishes. (McInnes, 1998).

Those having doubts about Hayek=s argument on informational deficits were persuaded by the grotesque misallocation of resources in the former Soviet Union. The critic, McInnes, noted that it was too late in Hayek=s life for him to see the vindication of his ideas at the time of the break-up of the Soviet Union. The experiences of the nations who have suffered under socialistic regimes have led to a

growing influence of Hayek's ideas in those nations. For example, a leading advocate of reform and privatization in Russia, Antoly Chubais, is a devoted follower of Hayek. Indeed, he occupies, currently, a high place in the Russian hierarchy. In China and elsewhere there are people sympathetic to Hayek's views.

Hayek's demonstration of how and why a central plan is incompatible with political and cultural freedom is equally convincing to McInnes. Hayek argues that the making of an economic plan involves the choosing between conflicting ends-different needs of different people. When these conflicts arise, they must be resolved. The experts empowered by the central planning authority are in a position to decide which of the conflicting ends are to be given preference. With central planning, the resolution of the problems and conflicts are delegated to these experts. Hayek notes that delegation in these instances means that some authority is given power to make, with the force of law, what to all intents and purposes are arbitrary decisions (Hayek, 1976). In other words, the freedom of the individual is lost and delegated to the collectivist authority. McInnes expresses this idea by saying that this process delegates decision from divided parliaments to arbitrary bureaucrats.

What are the points of controversy that remain between Hayek and his critics, given all these points of agreement? The principal controversy that remains is what McInnes calls the *slippery slope*. The central idea of *Serfdom* was that the process of governmental intervention becomes cumulative. Such interventions into the market order must, of necessity, beget further interferences. The idea captured by the notion of the slippery slope is that once we interfere with the market, we are on an irreversible path to socialism or worse. The counter argument advanced by McInnes and many others is that there is a middle, or a third way, This third way finds a stable compromise between what McInnes calls the uncontrolled market order and socialism, however it is defined. Hayek doubted that the third way could be a stable outcome. He wrote that, "The strongest support of the trend toward socialism comes today from those who

claim that they want neither capitalism nor socialism but a middle way or third way.@ He despairs of achieving such a third or middle way, arguing that once license is given to the politicians to interfere in the spontaneous order of the market for the benefit of particular groups, they cannot deny concessions to other groups (Hayek, 1979, p.150-151).

The argument for the third way seems eminently reasonable on its face. There is virtually no agreement for the desirability of the two extremes of an uncontrolled market order or for socialism. (Dedicated socialists or libertarians are extremely rare these days.) McInnes notes that Hayek himself would tolerate a level of government intervention that would make Milton Friedman blanch (McInnes, 1998). Hayek made it quite clear in the firsts chapter of *Serfdom* that he was not opposed to all economic interventions by government. He points out later that there may be a beneficial role for government, such as the provision of parks, museums, etc. He also favors the assurance of a minimum sustenance for all. Presumably, this would involve some non-earmarked payments in cash or in kind based on the perceived needs of the recipients.

Hayek would draw the line; however, when the coercive powers of government are used to insure that particular people get particular things This involves unequal treatment of different people which is irreconcilable with a free society. More generally, Hayek argues that the kind of welfare state that aims at social justice becomes primarily a redistributor of income, and is bound to lead back to socialism and its coercive and essentially arbitrary methods (Hayek, 1960).

Evidence on the Third Way

Here a subtle distinction must be made. The slippery slope idea that is refuted by McInnes has it that once one interferes into markets, there is no possible chance of reversal. That is, we can not eliminate governmental interferences and revert to private markets. The evidence clearly does not support this idea as pointed out by McInnes. The movement toward socialism, embodied in the U.S.

national energy policy, was terminated by the stroke of a pen in 1981 when President Reagan assumed office. Milton Friedman has noted that the movement toward socialism, instituted by the Labor Party in Great Britain after World War II, was arrested after a relatively brief period by the strong freedom impulses of the British people. Indeed, long incumbencies of the Thatcher government in Britain, the Kohl government in Germany, and the Reagan Administration in this country did serve to reverse the movements toward socialism, temporarily, at least. It is possible, therefore to reverse the trend for a time. The more important question is what is the status of matters at the present day? Have we reached a stable livable third way or are we still on a slope, slippery or otherwise?

The third way argument has proved to be rather popular politically. In Europe, this idea goes under the title of Social Democracy. Great Britain and Germany, in recent years, have elected governments that purport to follow the third way. In this country, President Clinton has attempted to distance himself from traditional Democratic policies that support ever increasing governmental intervention into private markets when he solemnly intoned in a State of the Union Address that the era of big government is over. By this, he too purports to follow the third way. Have these governments moved their nations to a stable and ideal compromise between free markets and socialism? If this were the case, these political leaders should be satisfied with the status quo. What is the actual situation?

First, as Eliot Abrams points out in an extremely perceptive article in *Commentary*, the wonderful vagueness of the term itself has been of immense utility, conjuring up as it does some magical midpoint between left and right that does not obligate the individual invoking it to be very clear about specifics (Abrams, 2000). McInnes, for example, argues that there must be such a point, but offers no specifics. This lack of specificity is not surprising, given the experience in the third-way nations.

A German writer argues that the universal welfare state in a very wide sense is at the core of the social democratic philosophy. This in German is called *Ader Vater Staat* that is, the state as a father taking care and acting always in the interest of his children. This same idea is expressed in Britain as the Nanny State. Both are names for the complete welfare state that Hayek found to be the modern embodiment of socialism. This writer examined the writings of Anthony Giddens, the leading theorist for the third-way policies, as supposedly followed by Prime Minister Blair. He concludes from these writings that the third way model do not describe a new chapter in social thinking and ideology. He argues that the starting point of the third way adherents is not the freedom of the individual, but rather collectivist ideas that are alive and well in the background of socialist thinking (Watrin, 1999).

The above ideas are reinforced by a document signed by Prime Minister Blair and Chancellor Schroeder of Germany that reads, "The State should not row but steer. It should not provide the wherewithal but determine the direction. It will no longer pay for things but will tell people what to do" (Dahrendorf, Ralf (1999)). The Social Democrats in these nations talk of reforming the welfare state to meet the criteria of social justice. According to Watrin, this means that social democrats want to keep welfare spending, and that they reject the libertarian position to privatize large parts of the welfare state. This would leave, only, a minimal safety net for those who cannot care for themselves.

The Social Democrats in these nations and, as we will see, their counterparts in this country have adopted an interesting strategy. A British writer, John Blundell, concludes that in practice, the Blair Government in Britain has been a curious mix of interfering authoritarianism and pro-enterprise liberalism. Indeed, some of their policies are more radical than the Conservative Party that preceded them. One outstanding example was trying to put the DNA of all offenders on file but other economic measures, such as the

contracting out of the management of public schools and the introduction of road pricing, were pursued (Blundell, 2000).

The other shoe drops, however, by the introduction of many measures taken directly from the left wing authoritarian handbook. For example, Blair introduced, for the first time, legislation for a national minimum wage. Blundell complains about what he calls the Labour Party's grotesque regulatory impulse, whether it be beef, eggs, passive smoking, unpasteurized milk, or the speed at which cars may be driven in television commercials. In addition, there are certain areas of health, education and welfare, Conservative Party policies of diversity, choice and individualism have been replaced by uniformity, state control and bureaucracy (Blundel, 2000).

In Germany, also, there have been movements away from collectivism, but these can best be characterized as baby steps. Chancellor Gerhard Schroeder did make reductions in the tax level. The marginal rate on income will fall from 51% to 42%, and corporate taxes will be reduced to 25% from 40%. Most arresting is the elimination of the capital gains tax on the sale of corporate assets. The reason that the steps are babyish is that it will take until 2004 before these billions trickle down from the government coffers (Joffe, 2000). With Germany's parliamentary system of government Schroeder could be long gone by then. The article in praise of these steps, by the editor of a leading Germany newspaper, points out, also, that Schroeder hasn't even begun to tackle one of the worst German economic diseases, namely, the merciless rigidity of labor and housing markets. To discharge a long-serving employee for incompetence may result in a severance payment that might reach six figures. Schroeder's answer to double-digit unemployment rates is an Alliance for work. Among the collectivist remedies is to cut the workweek, increase public sector investment and expand government-run labor-market programs. We see here, as in Britain, corroboration of Watrin's argument that collectivist ideas are alive still in the background of third-way thinking.

President Clinton does purport to follow the third-way. In fact, he proclaimed in his 1998 State of the Union message that we had found a third way. In his 1996 message, he had proclaimed that the era of big government is over. Was this a genuine movement toward a third way or was it simply a political maneuver? According to Abrams it was a bit of both, but probably more the latter than the former. Those on the left started to acknowledge that social problems embraced by the liberals had failed to solve those problems (expounded in magazines such as the *New Republic* and the *Washington Monthly*). After a decade the political genius of Bill Clinton did appropriate these conservative-winning ideas for liberalism. Abrams concedes that the maneuver was not entirely cynical nor have its consequences been negligible. But if the third way has not been entirely a cynical maneuver, it has certainly been calculated to reap the maximum political advantage for the Democratic Party. The vagueness of the term mentioned earlier adds to this advantage (Abrams, 2000).

Abrams further argues that, in light of the damage done to American society by liberal ideas, one might argue that it is worth paying the price in cynical partisan warfare for the sake of a more centrist Democratic Party. He concedes that the party has moved center-ward by some measures. But he insists that this is true only by some measures and, in a great phrase, by dint of the personal prestidigitation of the >triangulating= Bill Clinton. In other words, this is a bit of magic. Abrams concludes, however, that by other measures, the heart of the party remains on the Left and talk of a third way serves only to disguise the fact (Abrams, 2000). (Note the similarity between the political experiences in the U.S., Germany and Britain.)

Empirical Evidence

The empirical evidence strongly supports this conclusion. Despite the talk of the end of big government by Clinton, federal receipts as a percentage of the Gross Domestic Product (GDP) have increased

during every year of his administration. In 1992, receipts were 17.7% of GDP. They rose in 1999 to 20.3%, about the same level they were at in 1945, the year that World War II ended. This year (2000), they have risen to about 20.6%. In fact, all of those percentages represent a post 1945 peacetime record. By comparison, between 1945 and 1992 these percentages averaged 18.6% of GDP. In addition, the percentage of national income going into federal receipts rose, similarly, during the Clinton Administration. In 1992, this percentage was 22.4%. By 1999, it had risen to 25%. And so, a full quarter of our national income goes into the federal coffers.

It is true that the percentage of GDP going to federal expenditures has dropped, markedly, in recent years. In 1991 that percentage was 23.1. It has been in a steady decline since that time amounting to 19.1% in 1999. This decline has been caused by the exuberant economy that shows little indication of slowing down, as this is written. This has caused a significant federal surplus to accrue. In July 2000, the Congressional Budget Office estimated the surplus in the fiscal year ending in September of that year to amount to an incredible \$232 billion. Abrams captures the importance of this by noting, "Americans are now paying more in taxes than their government needs to do what it is doing." A true third way approach would dictate that there be a tax reduction to return some of these funds to the taxpayer thereby reducing the scope of the federal government. The Clinton Administration, including Vice-President Gore, firmly resists such a course of action. The excuse given is that it is necessary to pay down the Federal debt. But the debt's share of GDP has fallen to 34.9% this year from a 40-year high in of 49.2% in 1995 (Abrams, 2000).

In reality, the politicians are casting covetous eyes on the surplus to fund new programs. Clinton's State of the Union messages in recent years are heavily larded with proposals for new programs. This year (2000) Mr. Clinton and the Congress are agreeable to increasing domestic discretionary spending by 7%, which is triple the rate of inflation. Vice-President Gore has, by his own account, proposed

\$400 billion in new spending. Even the Republican aspirant to the Presidency, Texas Governor George W. Bush, would spend \$120 billion more in five years. (In fairness, though, Mr. Bush has made tax reduction a part of his program.) Abrams summarizes this well when he writes that today, with the Treasury awash in revenue, big government *Ca/k/a* tax and spend *Cis* back with a vengeance (Abrams, 2000). Somehow, the third way got lost along the way.

Conclusions

The concept of a third way is used to refute Hayek's thesis that government interferences, inevitably, move us toward socialism. This is an appealing, if not seductive thesis. Should not reasonable people seek livable and stable compromise between a relatively uncontrolled market order and socialism? In practice, of course, we are always at some point that we could call the third way. The important question, however, is whether a point can be found that is not a temporary stopping place en route to the socialism that Hayek feared and predicted. In the last decade, we have had empirical testing, of a sort, of the third way thesis. The U.S., Britain and Germany have elected political leaders that purport to follow the third way. The experiences in these countries go far to confirm the basic argument of Hayek.

In all three countries, as described above, there have been modest, but not trivial, movements toward free markets. In these countries, however, there have been the proposals or adoptions of policies that trace a trajectory down the well-trod path toward socialism as redefined by Hayek. After approving the welfare reform policies of the Republican Congress, President Clinton keeps calling for more federal programs as does his Vice-President aspiring to the presidency. Prime Minister Blair in Britain has reversed some of Mrs. Thatcher's policies while pursuing more regulation with a vengeance. In Germany, Chancellor Schroeder has proposed tax cuts that will not take effect for some years. His remedies for high unemployment, however, are more governmentally sponsored programs. In the U.S, data show that federal tax revenues as a

percentages of GDP and national income have risen steadily during the Clinton Presidency. Indeed, the percentage of GDP is at an all-time peacetime high and greatly exceeds the 1945-1992 average. This flies in the face of any notion that stable third way compromises have been reached in these nations.

It is clear that the third way notion carries great electoral appeal here and in Western Europe. The more serious question asks whether those advocating the third way are sincere in finding that magical point or whether they are using the idea as primarily an election gambit. The recent experience seems to confirm that the latter proposition appears to be true. The third way rhetoric appears to offer, at best, political cover for what, in the main, is the continuance or extension of socialistic type policies. Abrams summarizes it nicely when he concludes that the heart of the (Democratic) party remains on the left and talk of a third way serves only to disguise the fact (Abrams, 2000).

In sum, there is still a downward slope toward socialism, although the degree of slipperiness may vary. Also, it is possible to deviate from that slope for short periods, as we have seen. In mathematical terms, the slope of the long-term trend line is always downward, but there are cyclical variation around that line that temporarily reverse that slope such as we have seen in the three countries. It is doubtful, however, that we will approach anything like total socialism in any sense of the word. To use mathematical ideas again, the trend line downward is probably asymptotic to the axis representing total socialism. In words, this means that the downward trend line will always move more ever closer to the line but never reach it. It is like receiving an offside penalty inside the five-yard line. The team keeps approaching the goal but can not score a touchdown in this manner. The net result, again, is that Hayek=s basic thesis is amply supported by factual experience.

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