

The Political Economy of Liberty and Money

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Introduction: The Foundation of Modern Liberty

On a quiet morning in December 2010, a young street vendor named Mohammed Bouazizi set himself on fire in protest against police corruption in Tunisia. His desperate act ignited a wave of uprisings across the Arab world—an eruption of hope that democracy and freedom would finally prevail. It was called the Arab Spring. But just as quickly as the flames of revolution spread, they were extinguished. By mid-2012, authoritarian regimes had reasserted control, and the promises of liberty had faded into repression once more. Winter returned after spring.

The Norwegian Nobel Committee awarded its Peace Prize to Aung San Suu Kyi of Myanmar (Burma) in 1991. Praising her non-violent struggle for democracy and human rights, the Committee wished “to honour this woman for her unflagging efforts and to show its support for the many people throughout the world who are striving to attain democracy, human rights and ethnic conciliation by peaceful means.” A quarter of a century later, in 2015, Aung San Suu Kyi won a landslide election victory; Myanmar embarked on a path to democracy. But the initial hope and enthusiasm were short lived. Under the cover of Aung San Suu Kyi’s leadership, the military committed genocide, and in February 2021 they took back power, brutally killing thousands of opponents and pushing the country into civil war. What went wrong?

In 1919, Germany adopted the Constitution of Weimar. Praised as the most democratic constitution in the world, it declared that “the freedom of the person is inviolable” (art.114), “all Germans are equal before the law” (art. 109), and claimed respect for the principles of justice with the purpose of ensuring a dignified existence for all” (art. 151). Less than 13 years later, hyperinflation had destroyed most of the financial wealth of the country, austerity had pushed unemployment to over 30 percent, justice seemed to be ignored, and the Nazis took over. And yet, many decades later Germany had become a decent democracy. What went right?

These episodes reveal a deeper pattern: liberty’s survival depends not merely on constitutional declarations, democratic elections, or an international human rights machinery, but on underlying social and economic structures that make the norms of individual freedom both comprehensible and sustainable.

The central question of this book is therefore not why people desire freedom, but how it became possible to think what no one had thought before—that individuals are born free and equal, and that individual liberty should define what it means to be human.

What generates the widespread acceptance of modern liberty as a valid norm? By answering this question, I design a foundational theory of liberty. Without such theory it is impossible to understand, why attempts to overcome authoritarian rule and install respect for human rights have failed; nor can we design strategies for promoting liberty.

Let me share what motivated my quest to write this book. For decades I have supported democracy, human rights, and peace in Burma/Myanmar. Yet, I gradually came to see that the norms of individual liberty were not widely understood or shared in that country. In 1994, after decades of civil war in Myanmar, the Kachin Independence Army (KIA) concluded a ceasefire agreement with the Burmese military. I joined a small delegation of international observers witnessing the local arrangements. Northern Burma had been sealed off from the world for nearly forty years, and our journey to Lashio—where we met the local commander, who ranked third in the ruling military junta—was arduous. Upon arrival, the General greeted us: "You've had a difficult trip. Help us secure loans from the World Bank so we can improve our transport system." I replied: "Release Aung San Suu Kyi from house arrest and respect human rights. Then you can apply for funds." The General scoffed: "Human rights? That just means women can lie topless on the beach." When I raised the issue of forced labour constructing a road which I had witnessed on the way, he dismissed me: "We have no money, and this is how we have built roads for thousands of years."

What seemed normal and justified to this general—mobilizing citizens for state projects, dismissing individual rights as Western decadence—revealed a fundamentally different normative framework. He was not simply rejecting human rights; he could not think within their logic. This encounter showed that the concepts of individual liberty cannot be taken for granted.

Most people in that society think in terms of hierarchy. This is obvious for the military. Yet the military was not alone in its normative blindness. While many in Myanmar called for democracy, few grasped that democracy, human rights, and individual liberty rest on the foundational principle that all people are born free and equal. When the military committed genocide in 2016-17, driving nearly a million Rohingyas into Bangladesh, even some of Aung San Suu Kyi's most fervent supporters told me: "We don't want them in Myanmar. They're Muslims; we're Buddhist." The norms of modern individual liberty – freedom and equality – were not widely accepted as valid or worthy of action — even among those who claim to defend democracy.

Modern liberty and human rights are a historical construction rather than naturally given. Not everyone believes that we are or ought to be equal before the law, that individuals ought to be protected against authorities, or that collective choices ought to be made democratically. These ideas did hardly exist 500 years ago. For more than 10 000 years, people accepted

hierarchy as the default mode for their relations. Yet, to be clear, this transformation was neither linear nor inevitable; hierarchical and contractual orders have coexisted throughout history, and reversals remain possible when material insecurity undermines reciprocal relations.

This book argues that modern individual liberty and the monetary economy co-evolved through a process of reciprocal transformation. In ancient and traditional societies, hierarchical structures allocated resources and defined social roles. Hierarchy prescribed not merely what people did but who they were: identity, status, and life possibilities flowed from one's position within a collective order. Individuals conformed to assigned roles rather than designing their own lives or developing distinctive capabilities.

Commerce and markets began to erode this hierarchical determination. When individuals negotiated terms as equals, they exercised autonomy and created reciprocal obligations independent of inherited status. Scholars have observed this joint emergence of modern liberty and market society (Rosenblatt 2018). Milton Friedman famously claimed that "economic freedom is a necessary condition for political freedom" (2002, 9). Yet such observations do not explain why markets displaced traditional social orders, or, as Eric MacGilvray puts it, "why the language of freedom is now so closely associated with markets" (MacGilvray 2011, 56). Amartya Sen (1999, 6) argued that "the ability of the market mechanism to contribute to high economic growth and to overall economic progress has been widely - and rightly - acknowledged in the contemporary development literature. But it would be a mistake to understand the place of the market mechanism only in derivative terms. Freedom of exchange and transaction is itself part and parcel of the basic liberties that people have reason to value". Economic and human development requires a broader context than the ability to let the market mechanism contribute to high economic growth.

This book advances a monetary explanation that goes deeper than the conventional market freedom hypothesis. Let me explain again how I came to this understanding. I have pondered this question for years while working in Europe on creating a single currency—the euro—acceptable to all. Then, in 1996, I was invited as a ceasefire observer by the Karenni Democratic Revolutionary Party, a small ethnic resistance group in Myanmar. The group proved short-lived, but it produced a lasting insight.

I stayed in a village deep in Kayah State's jungle. One morning, my wife and I were served rice gruel for breakfast, and I suddenly asked our hosts: "Where did you get this rice? I haven't seen a shop in the village. What money do you use?" The answer was revealing: "We receive rice allocations from the Central Committee of the Karenni Democratic Revolutionary Party. We don't need money. Only the party leadership needs money—they get it by selling crops in Thailand and buying weapons there."

In that moment, I understood that democracy becomes meaningless when survival depends on political allocations, even from a party with "democratic" in its name. The monetary economy, I realized, forms the foundation of individual liberty. This became clearer when I travelled through official, military-controlled Burma. Although they had money—the currency is called kyat—it was dysfunctional. Inflation ran high, the currency was inconvertible, exchange rates were distorted, and people saved in US dollars or Thai baht instead. The insight that money, individual liberty, and democratic culture are intricately connected became the inspiration for this book.

Liberty as a norm

Liberty is primarily a normative concept. Only when the norm is considered valid does it make sense “to strengthen social arrangements for securing human freedoms—with norms, institutions, legal frameworks and an enabling economic environment” (UNDP 2000, 7). As my Myanmar experience demonstrates, defending human rights proves impossible when the norm of individual liberty lacks general acceptance.

What does "general acceptance" mean? All norms rest on the common knowledge of their validity. How does such common knowledge emerge? We must distinguish two mechanisms. First, someone conceives a functional innovation that others adopt for pragmatic reasons—a form of evolutionary selection where useful practices spread through imitation. However, different functions embody different norms. Hierarchical allocation of resources (e.g. a chief distributing grain to followers) embodies norms of authority and dependence; contractual exchange (e.g. merchants negotiating price) embodies norms of autonomy and equality. The function of hierarchy thus fits ancient collective liberty; the function of contracts fits modern individual liberty.

Second, because fulfilling functions requires communication and coordination, norms also emerge when people discuss their practices and articulate shared understandings. Norms emerge from repeated social practices—when people coordinate action within groups, they generate shared understandings of appropriate behaviour.

Medieval merchants exemplify this dynamic. Some merchants created promissory notes as a practical solution to the dangers of transporting coins over long distances. As this practice spread, merchants began discussing and debating: What makes a note valid? Who can endorse it? When must it be honoured? How should disputes be resolved? Through these discussions, merchants collectively articulated normative principles—transferability, enforceability, standardized terms—that had been implicit in their practices. They expected that agreements were binding. These expectations crystallized into normative principles—contractual freedom, voluntary obligations, and individual autonomy. Gradually these commercial norms expanded beyond merchant communities and defined individual liberty for all. Understanding this transformation—how credit obligations restructured social relations and how social relations were articulating the discourse of modern liberty—reveals

the pathway from ancient hierarchical societies to modern individual liberty and ultimately to human rights grounded in individual autonomy.

If markets, money and contracts lay the foundation for modern liberty, why do ancient and traditional societies stick to hierarchy and subordination of individual freedom? The answer is security in an environment of uncertainty. Especially in societies living close to the subsistence level, the need for safety and security explains why people voluntarily surrender to hierarchy and give up even limited margins of freedom. Where survival constitutes the dominant norm, hierarchy provides security. When the risks of disaster are perceived as relatively low, reciprocity of mutual help – as in my Karenni village – allows relative flat hierarchies. Nevertheless, surrender to the communitarian norms is paramount. When risks and uncertainties are high, steeper hierarchies with centralised resource management are preferable. I will demonstrate this logic with the example of pre-monetary palatial societies in Bronze Age Greece.

Contracts embody the interactional logic of modern liberty. When two individuals negotiate a contract, each remains free to accept or reject its terms. This reciprocal freedom constitutes their equality: neither can impose conditions unilaterally; agreement is required. They are equal because each is equally free to accept or reject terms. Their freedom makes them equal. Freedom and equality are therefore not independent principles but reciprocally constituting conditions. Throughout this book, liberty denotes their inseparable duality: one cannot exist without the other.

Money and Markets

The long road to modern liberty began in Greece with coined money's invention in the seventh century BCE. Coinage made exchange more efficient than barter and introduced equality as an alternative normative principle to the allocation of resources through step hierarchy. Aristotle struggled with the fact that in commercial exchange goods were of equal value - he called this arithmetic justice – while for society as a whole (geometric) justice meant hierarchy and slavery.

Coinage was quickly adopted in Athens for reasons I will discuss in a later chapter. It also contributed to the emergence of Athenian democracy and colonialism. But Sparta remained a powerful non-monetary economy because it replaced money with coercive institutions.

Why did money's egalitarian potential remain dormant? Because when money primarily served as a means of exchange, it was not yet able to provide a degree of security equivalent to the modern liquidity of credit money. Ancient economies did have techniques for managing liquidity, but they were based on the ruler controlling quantities—how much coin circulated, how much credit they permitted. Some individual lenders charged interest on loans, but these rates reflected individual creditworthiness, not a system-wide price for money. No central interest rate governed overall liquidity. Authorities set quantities; the market couldn't price money itself. This changed only with the Bank of England's creation in 1694, which introduced

the modern practice of managing liquidity through interest rates rather than quantity controls. But even today, many dysfunctional monetary economies operate like ancient economies because they have no financial markets for pricing the value of liquidity.

I call exchange paradigm the interpretation of money serving primarily as a means of exchange. It dominates standard neoclassical economics and attributes market expansion to utility maximisation—ultimately, to unlimited wants. This explanation is inadequate because it treats scarcity as an intrinsic property of resources rather than as a relational outcome of supply and demand. At the micro level, scarcity appears as excess demand for particular goods. In monetary economies, however, the scarcity of money itself systematically generates scarcity across markets, producing buyers' markets, competition, and pressure to expand exchange. Monetary scarcity is inseparable from credit and interest rates. The central claim developed in this book is that credit contracts are the primary driver of market expansion.

Contractual practices remained limited until money evolved beyond spot exchange. Ancient coinage facilitated commerce whilst leaving hierarchies intact. The crucial transformation occurred during the late medieval financial revolution, when credit became money through innovations like bills of exchange, negotiable debts, and banking operations. Credit money made contractual claims liquid, transferable, and enforceable across time and space, generating a continuously expanding web of contractual relationships that both required and reinforced the norms of individual autonomy and equal freedom.

During the Renaissance, and more specifically during the Little Ice Age when climate change caused huge uncertainties, liquidity management emerged as an alternative to hierarchical insurance. Money became an instrument for managing risk and uncertainty. This function of money is better described by the contract paradigm, as I will explain in chapter 3. The contract paradigm differs from the exchange paradigm by assigning constitutive roles to uncertainty and risk aversion. In this paradigm uncertainty is constitutive because contracts are necessarily incomplete.

Contracts, money and rights

The diffusion of contractual practices also transformed the nature of rights. This is important because modern liberty is rights-based. In traditional societies, social order is predominantly organised through hierarchical relations of authority. Rights in such settings are not generated through reciprocal agreement but are granted from above as commands issued by rulers, chiefs, or sovereign authorities. These command-based grant-rights derive their validity from position and power rather than from mutual recognition among equals. Authority precedes entitlement: individuals hold rights insofar as they are permitted to do so by those who govern. Law in this sense functions primarily as an instrument of command, stabilising expectations through obedience rather than through claims grounded in consent.

By contrast, a contract-based economy rests on horizontal relations among formally free and equal agents. Here, rights emerge as claims generated by mutual agreements—most clearly

in private contracts, but ultimately also in the social contract that constitutes political authority itself. Claim rights are not permissions granted by rulers but entitlements that arise from reciprocal commitments and are recognised and enforced by institutions. Human rights represent the generalisation of this contractual logic: they articulate universal claims that individuals hold vis-à-vis political authority by virtue of their equal standing as human beings. Human rights are not explicit bargains, but universally claimable entitlements grounded in reciprocal recognition among free and equal persons.

This distinction between command-based and claim-based rights has a direct monetary analogue. Hierarchical orders tend to rely on money as an instrument of command: coinage functions primarily as a unit of account and means of exchange, facilitating exchange while remaining conceptually separable from underlying social obligations. By contrast, a contract-based economy is structured around credit relations. Here, money emerges endogenously from contractual claims and promises—debts, loans, and deposits—whose validity rests on mutual recognition rather than on unilateral decree. Credit money thus presupposes claim rights: it is a system of transferable obligations anchored in trust, enforceability, and institutional recognition. The transition from coin-based exchange to credit-based monetary systems therefore mirrors the broader transformation from hierarchical grant rights to contractual claim rights, and it is this shift that underpins both modern market economies and the universalisation of human rights as claims held against political authority rather than permissions granted by it.

In the following chapters I will first go deeper into the theoretical foundations of my model of liberty transformation. Several chapters have technical annexes to support the rigour of the arguments made in the main part of the chapters.

Part I lays the theoretical foundations. Chapter 1 clarifies different concepts of liberty, distinguishing ancient collective freedom from modern individual autonomy and examining contemporary debates (Berlin, Pettit, Sen) within the modern framework and how they match with Constant's distinction of the liberty of the ancients and the liberty of the moderns.

Chapter 2 addresses the question how liberty, conceived as a normative ideal, can generate actual social facts? How do norms translate into institutions that structure behaviour? This question is essential for explaining the transition from ancient to modern societies—a transition that positivist economists like Milton Friedman considered beyond economic analysis insisting on a strict separation between positive (what is) and normative (what ought to be) questions. I reject this separation, demonstrating that norms and facts co-constitute each other through social practices and speech acts that create institutional reality.

Chapter 3 describes the metamorphosis of money and elaborates the contract paradigm. It analyses ancient money which functioned primarily as a means of exchange—facilitating spot transactions as in barter. Modern money serves as a means of payment discharging obligations over time. This distinction matters because the payment of money provides

certainty of discharging debt contracts. Money then has utility that is larger than increasing the efficiency of barter. This utility has a price – the interest rate. We shall see that this utility is the driver of economic development and propagates the norms of contracts and liberty across the world.

The contract paradigm explains why modern societies have grown faster than traditional ones and why individual liberty's norms are more deeply embedded in economically developed societies. Yet this relationship is not deterministic. Economic crises that shrink material capabilities can prompt reversion to hierarchical authority—as the Great Depression spawned fascism and contemporary economic anxiety fuels authoritarian populism. Modern liberty requires both normative commitment and material conditions; neither alone suffices. My purpose is not to write liberal theory or monetary history but the theory of modern liberty's institutional foundations.

Part II traces this transformation historically, examining how medieval and early modern Europe developed the financial innovations—bills of exchange, negotiable instruments, banking systems, limited liability—that created credit money and contractual liberty. Chapter 4 examines how coinage—the first standardised form of money—contributed to the emergence of ancient collective liberty in Greece.

Chapter 5 traces a crucial transformation driven by an unexpected catalyst: how late medieval climate disruptions (the Little Ice Age, 1570-1720 CE) generated economic insecurity that, I argue, created unprecedented demand for financial instruments capable of managing risk across time and space. Harvest failures, trade disruptions, and demographic crisis spurring merchant communities to develop financial innovations (bills of exchange, negotiable debts, banking operations) that transformed money from a medium of spot exchange into a system for creating, transferring, and discharging obligations over time. This credit revolution laid the institutional foundations for both capitalism's expansion and modern individual liberty's emergence, demonstrating that the two developments were not merely correlated but causally intertwined.

Part III examines the emergence of the modern state as both response to uncertainty and as enabler of the monetary economy in early modern Europe. Two political philosophers mark contrasting approaches to this transformation. Chapter 6 demonstrates that Thomas Hobbes was the first thinker to construct a theory of sovereignty grounded in the logic of credit money and contractual obligation. Hobbes understood that monetary debts create enforceable claims between individuals, and he used this contractual model to explain political obligation: just as creditors hold claims against debtors, the sovereign holds authority through a social contract conceptualized as mutual promises among individuals seeking security. His theory thus reflected the emerging world of contractual relations and credit money.

Chapter 7 presents a paradox: John Locke's political philosophy became foundational for liberal individualism and modern economic thought, yet his monetary theory was rooted in the metallistic conception of money as commodity rather than as credit instrument. Locke's

advocacy for full-bodied coinage—money as stored precious metal rather than as claims—contributed to England's severe financial crisis of the 1690s. Despite this economic failure, or perhaps because of it, Locke's political philosophy proved enormously influential for the Whig-liberal movement and established conceptual foundations for what would become neoclassical economics, with its emphasis on individual property rights and market exchange rather than on credit relationships and monetary institutions.

In the final chapter 8, we will return to the present. Why does individual liberty face renewed challenge from authoritarian populism? Can liberty survive in an uncertain world of climate change, financial crises, and technological surveillance? Understanding how modern liberty emerged through specific institutional foundations—and recognizing that hierarchy still appeals when uncertainty threatens material security—may be essential for ensuring that individual freedom and equality survive the 21st century's challenges.