

## TWO THEORIES OF ECONOMIC LIBERALISM

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Within the Anglo-American world, economic liberalism is generally viewed as the intellectual offspring of Adam Smith, and neoliberalism its sole contemporary heir. But the development of economic liberalism also draws important ideas from G. W. F. Hegel, or so I shall argue in this paper. Hegel's work on economic liberalism initially and most directly influenced German-speaking political economists it's true, but this work had a more subtle impact on many English-speaking political economists later too, for a generation of these were heavily influenced by their German-speaking teachers.<sup>1</sup> And just as economic liberalism has not just one progenitor but two, it also has not one contemporary offspring but two: the other is called ordoliberalism, and while neoliberalism gets all the attention in the English-speaking world, ordoliberalism has been far more influential in the German-speaking world. But like many theories that can trace their inspiration to the same source, each of these contemporary versions of economic liberalism is very different. Indeed, each sees itself as embodying a different central defining metaphor. From Smith, neoliberals took the idea of the invisible hand, although I am going to argue that contemporary advocates of invisible hand theory have largely misconstrued or at the very least overstated the significance of this metaphor. From Hegel, ordoliberals took the idea of the civil society, and I am going to argue that the civil society is a much better metaphor not only for Hegel's but also for Smith's views.<sup>2</sup> What I am going to spend most of my time doing in this piece, however, is trying to

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\* Please note that this is the pre-copyedited version of the paper. The final published version may contain corrections, changes, additions or deletions, and should be considered the more definitive version of the paper as soon as it appears.

<sup>1</sup> See generally Lisa Herzog, *Inventing the Market: Smith, Hegel, & Political Theory* (Oxford: Oxford University Press, 2012).

<sup>2</sup> A similar point with regard to Smith and ordoliberalism is made by Herzog in *Inventing the Market* at p. 6 n. 22.

bring ordoliberalism more generally into the light—I will argue that by comparing and contrasting the views of Smith and Hegel or at least between how Smith and Hegel tend to be currently (mis)understood, we can better understand both the roots and the nature of these two contemporary incarnations of economic liberalism. And this, in turn, brings some interesting and important features of these two contemporary theories into view. Indeed, I will argue that ordoliberalism, not neoliberalism, is the better and more coherent instantiation of economic liberalism. But first, let's take a closer look at exactly what economic liberalism is and the context in which this attitude toward economic activity arose.

## I.

The rise of economic liberalism largely coincides with the rise of economics as a discipline. For hundreds of years, the primary economic activity of almost every society that had formed itself into a nation was agriculture, at least if one excludes war and conquest as an economic activity. But beginning with the fifteenth century, more and more commercial activity started to involve the production of finished goods, making trade in these and in the raw materials on which they were based more and more important. By the end of the fifteenth century, the idea that agriculture was the only economic activity worth thinking about began to give way to what Smith calls mercantilism, the idea that there is such a thing as national wealth, that this is measured by the stocks of gold and other treasure held by a nation and by its balance of trade, and that these measures of economic activity are accordingly to be maximized.<sup>3</sup> Now Smith would go on to rail against mercantilism (indeed, the title of the book for which he is most famous suggests that the mercantilism and its view of national wealth was his primary target), but there was one other common aspect of how economic activity was organized at the time that he also attacked. This was the guild system, which arose alongside mercantilism because non-agricultural commercial activity involved many small shopkeepers who were members of various guilds that set price and quality

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<sup>3</sup> See generally, Mark Blaug, *Economic Theory in Retrospect* (Cambridge: Cambridge University Press, 5th ed. 1996), ch.1; Joseph A. Schumpeter, *History of Economic Analysis* (Oxford: Oxford University Press, 2 1954), pt. 2, ch.7, pp. 335-376; Jacob Viner, "English Theories of Foreign Trade Before Adam Smith," *Journal of Political Economy* 38 (1930): 249-301.

standards for the goods their members produced and sold and controlled access to the profession. One had to be a member of the guild to deal in goods of that kind, for the government, seeking the favor of the rising merchant class, would protect the guilds from external competition through what Smith calls "the policy of Europe" and, more formally in England, through the Statute of Apprenticeship.<sup>4</sup> Economic activity in Smith's day was accordingly both privately and publically regulated—it was privately regulated by the guilds in the sense that they set price and quality standards and prevented free competition from undermining these standards by strictly controlling entry into the profession. It was publically regulated by the government in the sense that the government gave the guild's regulations the force of law and in the sense that mercantilism entailed protectionism: because national wealth was thought to depend in large part on the balance of trade, much legislation had been enacted that effectively prohibited or at least severely limited the importation of certain foreign goods, the most infamous example of this being grain, whose importation was heavily restricted under the now-infamous Corn Laws.<sup>5</sup>

This, then, is the context in which Smith's views were formed and through which they must be interpreted and understood. A wide range of territory that involved what Smith understood to be economic activity was heavily regulated; monopoly and monopoly power was rampant if not expressly granted or at least protected under law; competition both foreign and domestic was often effectively suppressed and as a result innovation and entrepreneurship were difficult if not impossible. But the main problem with the way economic activity was understood at the time is that this understanding was unsystematic, incomplete, and sufficiently mistaken that it often produced counter-productive policies. In the face of this,

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<sup>4</sup> See Smith, *Wealth of Nations*, bk. 1, ch. 10, pt. 2, pp. 136-165.

<sup>5</sup> I should note that there was also a national security justification for legislation like the Corn Laws. The argument was that the country should not be dependent on foreign sources for food and other critical goods and raw materials. To ensure the development and maintenance of a healthy domestic source of supply, certain industries accordingly had to be protected from foreign competition. Of course, there is a national security as well as an economic response to this argument: the national security response is that the more countries become dependent on one another, one for a source of supply and the other for the income that export of this supply brings, the less likely the two countries are to go to war. Indeed, this latter argument is one of the key motivations for the formation of the European Union.

Smith "was the first to try, with remarkable success, to arrange the subjects of economics into an organized discipline."<sup>6</sup> His objective was to clear up a lot of existing confusion about how an economy operated and how to tell if it was operating well, and to suggest why we might consider changing certain prevailing policies and practices to ones that seemed more sensible given the interests of a wider segment of society than the segment that was technically in charge.<sup>7</sup> What he developed was a theory about what should be the subject matter of economics, which included a theory about what made economies perform best, where best was understood as the greatest achievable amount of production given society's then existing resources. And so while it is true that Smith railed against the guild system and against international protectionism in favor of a system that allowed free competition both within and between nations, and Smith's views were therefore liberal or rather "liberalizing" in this sense, viewed in their proper context his views are best seen as a reaction to the almost smothering degree of control over economic activity exercised at the time by both private and public regulators. His was not an attempt to start a movement, or to replace one form of extremism with another—he was arguing for a middle ground, not the disestablishment of economic order in favor of what might be considered an economic free-for-all, despite the fact that this is what contemporary neoliberals would seem to have us think.

Indeed, if one looks at Smith's work as a whole, one cannot help but agree with Jacob Viner, one of the founding figures of the what I think is fair to characterize as the relatively conservative free-market "Chicago School" of economics, who said long ago:

Adam Smith was not a doctrinaire advocate of laissez faire. He saw a wide and elastic range of activity for government, and he was prepared to extend it farther if government, by improving its standards of competence, honesty, and public spirit showed itself entitled to wider responsibilities. .

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<sup>6</sup> Léon Walrus, *Elements of Theoretical Economics*, trans. Donald A. Walker and Jan van Daal (Cambridge: Cambridge University Press, 2014), p. 4.

<sup>7</sup> See, e.g., Smith, *Wealth of Nations*, bk.1, ch. 10, pt. 1, pp. 142, 145; bk. 1, ch. 11, pt. 3, p. 287; bk. 4, ch.3, pt. 1, p. 527 (all criticizing monopolies, monopolization, and other restraints on trade); bk. 4, ch. 8, pp. 694-717, esp. p. 697 (criticizing mercantilism for ignoring the poor, indigent, neglected, and oppressed).

. He helped greatly to free England from the bonds of a set of regulatory measures which had always been ill advised and based on fallacious economic notions, but he did not foresee that England would soon need a new set of regulations to protect her laboring masses against new, and to them dangerous, methods of industrial organization and industrial technique. Smith was endowed with a more than ordinary allotment of common sense, but he was not a prophet. But even in his own day, when it was not so easy to see, Smith saw that self-interest and competition were sometimes treacherous to the public interest they were supposed to serve, and he was prepared to have government exercise some measure of control over them where the need could be shown and the competence of government for the task demonstrated.<sup>8</sup>

## II.

In many ways, although he was writing some 50 years later, Hegel found himself in a world that looked very much like the one that Smith confronted, at least as far as management of the economy was concerned. In Germany mercantilism was called cameralism, and although some of the most important formative events of the modern era had now occurred (the French and American revolutions and the beginnings of the industrial revolution), the German-speaking world had not yet really changed.<sup>9</sup> To the cameralists,

the central problem of science was the problem of the state. To them the object of all social theory was to show how the welfare of the state might be secured. They saw in the welfare of the state the source of all other welfare. Their key to the welfare of the state was revenue to supply the needs of the state. Their whole social theory radiated from the central task of furnishing the state with ready means.<sup>10</sup>

Economic activity was accordingly heavily regulated and taxed; exports were favored over imports, which were heavily restricted; there was an obsession with the acquisition and hoarding of precious metals; and the economy was in general viewed as something which was to be managed by the state and by what Joseph Schumpeter called its "Consultant

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<sup>8</sup> Jacob Viner, "Adam Smith and Laissez Faire," *Journal of Political Economy* 35 (1927): 198-232, 231-232. For further argument on this point, see Herzog, *Inventing the Market*, ch. 2.

<sup>9</sup> For a general discussion of cameralism, its relation to mercantilism, and its continued dominance in Germany and Austria even after the influence of mercantilism had started to wane in England, see Karl Hauser, "Historical School and 'Methodenstreit'," *Journal of Institutional and Theoretical Economics* 144 (1988): 532-542.

<sup>10</sup> Albion W. Small, *The Cameralists* (New York: Burt Franklin, 1909), pp. viii.

Administrators" for the benefit of the elite rather than the population at large.<sup>11</sup> Although the cameralists claimed that the welfare of the masses and the welfare of the elite were tied together in a trickle-down sort of way, this welfarist connection existed only in theory and not in practice: the great majority of the population was impoverished while a small minority lived in luxury.<sup>12</sup> The position of those who were just managing to venture up and into a nascent middle class remained precarious.<sup>13</sup>

Reacting to this, Hegel introduced the idea of the civil society, a society that was not so easily subjugated by the wealthy and which put satisfying the basic needs of all people above satiating the often frivolous but apparently bottomless wants of the few. For Hegel,

Civil society is not merely the natural result of people's free and self-interested behaviour . . . it is a genuine form of society, a 'universal family' which makes collective demands on its members and has collective responsibilities toward them (PR § 239). As members of this society, individuals have the duty to support themselves through labour which benefits the whole, while civil society as a whole owes each individual the opportunity to labour in a way which provides a secure, respected and self-fulfilling mode of life (PR §238). This means that civil society is charged with the education of individuals for membership in it (PR § 239), and also collectively responsible for preventing them from falling into poverty, whether through their own improvidence (PR § 240) or through the contingencies of the market system. The poor in civil society are victims not of some natural misfortune, but of a social wrong (PR § 240).<sup>14</sup>

Accordingly, when Hegel proselytized for a "free market," what he meant was not an unregulated and unsupervised market, but rather a market that was open to all, one where not only contracts but also fairness would be respected and vigorously enforced, a market that was regulated by competition but was also supported by social programs that ensured that the many would not simply be exploited for the benefit of the few and then left to fend for

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<sup>11</sup> See Joseph A. Schumpeter, *History of Economic Analysis* (Oxford: Oxford University Press, 1954), p. 159-160.

<sup>12</sup> For a discussion of the contemporary resurrection of this argument, see Mark R. Reiff, "The Difference Principle, Rising Inequality, and Supply-Side Economics: How Rawls Got Hijacked by the Right," *Revue de Philosophie Économique/Review of Economic Philosophy* 13:2 (2012): 119-173

<sup>13</sup> See generally Murray N. Rothbard, *Economic Thought Before Adam Smith: An Austrian Perspective on the History of Economic Thought, Volume I* (Auburn, AL: Ludwig von Mises Institute, 1995), pp. 492- 494; Small, *The Cameralists*, pp. 1-20; Schumpeter, *History of Economic Analysis*, pp. 159-160.

<sup>14</sup> Allen W. Wood, "Editor's Introduction," in G. W. F. Hegel, *Elements of Philosophy of Right* (Cambridge: Cambridge University Press, 1991), pp. xviii-xix (the references in parenthesis are to the relevant section number's in Hegel's text).

themselves. Like Smith then, Hegel regarded both the state-run economy and complete freedom of trade as extremes; the health of a civil society required a middle course.<sup>15</sup> Like Smith, Hegel's approach to the regulation of economic activity was economic *liberalism*, not economic *anarchism*.

It is also important to recognize that economic liberalism was not only alive in Hegel as well as in Smith, it was actually Hegel and not Smith who made the first express connection between economic liberalism and political freedom, a key element of all theories of economic liberalism in the modern age. For Hegel, however, when he spoke of freedom he meant not freedom from constraint or "negative liberty" as Isaiah Berlin would later call it,<sup>16</sup> but the freedom to live a certain kind of life, the freedom to self-actualize,<sup>17</sup> the kind of freedom Berlin and everyone thereafter (including prominent Hegel scholars such as Charles Taylor) would later refer to as "positive liberty."<sup>18</sup> There are accordingly two senses in which Hegel's economic liberalism was "liberalizing" or freedom promoting: it argued for greater negative liberty in the sense that it advocated reducing certain specific kinds of constraints then in force on economic activity; and it argued for greater positive liberty in the sense that it did not simply advocate maximizing negative liberty; rather, it recognized that certain kinds of constraints were necessary if negative liberty was to be meaningful and to ensure that the market would enable people to live the kind of life that Hegel envisioned was *just* and not one that reduced to a war of all against all.<sup>19</sup> And as we shall see in a moment, this is the kind of political freedom that ordoliberalism tries to ensure; whereas neoliberalism makes the mistake of thinking of political freedom only in the negative liberty sense.

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<sup>15</sup> See *Ibid.* at p. xix.

<sup>16</sup> See Isaiah Berlin, "Two Concepts of Liberty," in *Liberty*, ed. Henry Hardy (Oxford: Oxford University Press, 2002), pp. 166-217.

<sup>17</sup> See *Ibid.* at pp. xi-xix.

<sup>18</sup> See Berlin, "Two Concepts of Liberty;" Charles Taylor, "What's Wrong with Negative Liberty," in *Philosophy and the Human Sciences: Philosophical Papers Volume 2*, (1985), pp. 211-229; Eric MacGilvray, *The Invention of Market Freedom* (Cambridge: Cambridge University Press, 2011), p. 174.

<sup>19</sup> See Herzog, *Inventing the Market*, p. 121: "For Hegel, negative freedom is highly valuable, but as it is potentially self-undermining rather than self-reinforcing, it needs to be supplemented by institutions that secure richer notions of freedom."

## III.

This common mistake by contemporary neoliberals, however, cannot be blamed on Smith. Smith saw his economic liberalism as purely economic. For while he did refer to certain kinds of government regulation of economic activity as violations of "natural liberty," by which he meant negative liberty or freedom from constraint, he did not make any larger connection between liberty in the economic sphere and liberty in the political sphere.<sup>20</sup> Indeed, he went out of his way to note that natural liberty (that is, negative liberty in the economic sphere) is subject to the restraints of justice.<sup>21</sup> In other words, negative liberty is *not* a moral end in itself, but rather a mere default position with regard to economic activity because it promotes economic efficiency. Economic efficiency, in turn, is a prudential goal, not (or at least not necessarily) a moral one, and therefore can be overcome by concerns of justice. Smith did not even think that natural liberty—in other words, negative liberty in the economic sphere—should be maximized, suggesting instead that this was not only impossible, it was also unnecessary, for a nation could enjoy wealth and prosperity even within an economic system that fell well short of "perfect liberty,"<sup>22</sup> which again indicates that he did not view natural liberty as a moral end in itself. Indeed, Smith did not even use the phrase "natural liberty" in *The Theory of Moral Sentiments*, which he surely would have done had he considered the idea a moral notion. So it was not Smith who moralized economic liberalism by connecting it to political liberty.<sup>23</sup> And even

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<sup>20</sup> See, e.g., Smith, *Wealth of Nations*, bk. 2, ch. 2, p. 353 (describing rules against accepting bank notes as a violation of natural liberty); bk. 4, ch. 5, p. 568 (describing rules prohibiting a manufacturer from but requiring a farmer to sell their goods at retail as violations of natural liberty); bk. 1, ch. 10, pt. 1, p. 162 (describing rules which prohibit laborers from one parish working in another a violation of natural liberty); and so on.

<sup>21</sup> See Smith, *Wealth of Nations*, bk. 4, ch. 9, p. 745.

<sup>22</sup> See Smith, *Wealth of Nations*, bk. 4, ch. 9, pp. 730-731.

<sup>23</sup> Which is not to say that Smith did not notice that economic liberty could promote personal autonomy—he did, and he also recognized that economic liberty could undermine it. See Herzog, *Inventing the Market*, ch. 6. But this does not turn Smith's concept of economic liberty into a political theory; on the contrary, it merely confirms that Smith saw the necessity of subjecting economic liberty



though Hegel did make such a connection, the real metamorphosis of economic liberalism from an economic theory to a full-blown political theory did not happen until much later.

The two great historical events that produced this metamorphosis was the Russian revolution and rise of fascism in Europe. Both of these events were populist reactions to widespread economic hardship, and while (most of) those inside these movements must have seen them as (at least potentially) liberating in some way, from the outside at the time and from every enlightened point of view thereafter they were anything but. They were rejections of the still largely unrealized and to some extent not yet even fully formed ideas of political liberalism, and constituted attempts to put a perfectionist political vision in its place, although a different perfectionist vision in each case.<sup>24</sup> Each in its own way, (socialism directly and fascism indirectly, through its imposition of a rigidly hierarchical structure on all aspects of social, religious, artistic, and economic life) also represented attacks on the free market system. And while the economic programs of these political viewpoints poured out of their political ideology, one can understand how outsiders might have seen the direction of causation here as potentially running the other way: if a rejection of economic freedom was the direct policy of these political movements, or even just an indirect effect of their more explicitly political policies, then any attempt to curtail economic freedom in the negative liberty sense must also have political effects. And once the idea that economic and political freedom were intimately connected in a causal way seemed to be borne out by events, economic liberals began to see even the smallest step away from economic freedom as a giant leap toward the totalitarianism or authoritarianism of either communism or fascism.<sup>25</sup>

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to the constraints of justice, constraints that had to come from outside the theory of economic liberty itself.

<sup>24</sup> For an extensive discussion of the differences between liberalism and perfectionism, see Mark R Reiff, "The Attack on Liberalism," in *Law and Philosophy*, ed. Michael Freeman and Ross Harrison (Oxford: Oxford University Press, 2007), pp. 173-210.

<sup>25</sup> See, e.g., F. A. Hayek, *The Road to Serfdom* (London: Routledge, 1944), esp. ch. 7. For later expressions of this same view, see Milton Friedman, *Capitalism and Freedom* (Chicago: University of Chicago Press, 1962), esp. ch. 1; Milton Friedman and Rose Friedman, *Free to Choose* (Orlando, FL: Harcourt, Inc, 1980).

What is interesting about all this is that shortly after becoming self-aware of what it saw as the consequentialist implications of economic liberalism for political freedom, economic liberalism as a movement split into two versions. One branch, now called neoliberalism, focused almost exclusively on the efforts of government to interfere with market operations, and saw itself as primarily advocating government non-interference in the marketplace as a way of protecting negative liberty. How strict this principle of non-interference should be, and even exactly how it should be cashed out, became a controversial topic, for early neoliberals still saw a major role for government regulation—they just feared anything that looked like economic central planning or the allocation of economic assets or government regulation of price or quantity decisions.<sup>26</sup> Later neoliberals, however, simply embraced knee-jerk obstructionism—they argued that government could do nothing better than the market, the creation of the market being viewed as a sort of *fait accompli* and in any event as something capable of existing outside government or any of its many tentacles. These later neoliberals were obsessed with maximizing negative liberty in the strictly quantitative sense, without regard to the quality of the negative liberty involved, because they saw the political liberty available in countries that adopted capitalism as their economic system as greater than those did not. From this point of view, then, any attempt at government regulation of the market was a step toward socialism.

But we will get to this particular metamorphosis—the change from a belief in government regulatory restraint to a belief in government regulatory abolition—in a minute. What I want to point out now is that while it is hardly ever mentioned in the English-speaking world, economic liberalism also had another offspring at the same time it gave birth to neoliberalism. Because of its focus on rule-based order, this offspring was called ordoliberalism, and while it shared the underlying economic viewpoint of economic

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<sup>26</sup> See Ludwig von Mises, *Interventionism: An Economic Analysis* (Indianapolis: Liberty Fund, 1998, 2011) (originally published in 1940), p. 19; Ludwig von Mises, *Liberalism* (Auburn, AL: Ludwig von Mises Institute, 2010), p. 76 (originally published as *Liberalismus* by Gustav Fischer in 1927); Ludwig von Mises, *A Critique of Interventionism* (Auburn, AL: Ludwig von Mises Institute, 2011), pp. 2, 4 (also originally published in 1927).

liberalism as well as the belief that the economic is political, operationally it could not have been more different in how it believed these underlying fundamental ideas should be instantiated. Like neoliberals, ordoliberals believed that government should not be engaged in central economic planning or setting prices or deciding what types or quantities of goods should be produced. But unlike neoliberals, ordoliberals did not focus exclusively on how government interference could interrupt the workings of the free market system. They realized that private parties could interfere with the workings of the free market too. To them, a free market meant a *competitive* market, or at least a market that was as competitive as it could be, and therefore anti-competitive practices by private parties were just as dangerous to political freedom as direct government planning of production. And if one is concerned about private anti-competitive behavior, one cannot rely solely on the market to prevent this—one must look to government regulation as a necessary element of any attempt to ensure that markets remain free in the relevant sense. "The social market economy obliges me," said the ordoliberal architect of West German reconstruction, "to focus my attention on, and to declare war against, all efforts to form cartels and against those aiming at retaliation of competition of whatever kind."<sup>27</sup> So while neoliberals opposed all attempts at government regulation, ordoliberals embraced government regulation that ensured the competitiveness of the market—only government regulation which did not do this was objectionable to them.<sup>28</sup>

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<sup>27</sup>Ludwig Erhard, *Prosperity through Competition* (New York: Frederick A. Praeger, 1958), p.117. The author was Vice-Chancellor and Minister of Economic Affairs for the German Federal Republic from 1948 to 1963.

<sup>28</sup> See Franz Bohm, Walter Eucken, and Hans Grossmann-Doerth, "The Ordo Manifesto of 1936," in *Germany's Social Market Economy: Origins and Evolution*, ed. Alan Peacock and Hans Willgerodt (London: Macmillan, 1989), pp. 15-26; Wilhelm Röpke, *The Social Crisis of Our Time* (Chicago: University of Chicago Press, 1950), pp. 227-235; Viktor Vanberg, "'Oduningstheorie' as Constitutional Economics—The German Conception of a 'Social Market Economy'," *Ordo* 39 (1988): 17-31; Henry M. Oliver Jr., "German Neoliberalism," *The Quarterly Journal of Economics* 74 (1960): 117-149; Walter Eucken and T. W. Hutchison, "On the Theory of the Centrally Administered Economy: An Analysis of the German Experiment: Part II," *Economica* 15 (1948): 173-193, 182-185; Viktor J. Vanberg, "Constitutionally Constrained and Safeguarded Competition in Markets and Politics," in *The Constitution of Markets: Essays in Political Economy* (London: Routledge, 2001), pp. 1-16, esp. p. 4; Ralf Ptak, "Neoliberalism in Germany," in *The Road from Mont Pelerin: The Making of the Neoliberal Thought Collective*, ed. Philip Mirowski and Dieter Plehwe (Cambridge: Harvard University Press, 2009), pp. 98-138; Gerhard Schnyder and Mathias Siems, "The Ordoliberal Variety of Neoliberalism," in *Banking Systems in Crisis: The Faces of Liberal Capitalism*, ed. Suzanne J. Konzelmann and Marc Fovargue-Davies (Abingdon: Routledge, 2013), pp. 250-268.

Note here that like neoliberals, ordoliberals also connected economic to political freedom through a consequentialist principle: their view was that anti-competitive behavior produced governments that were more likely to reduce political freedom. And note also that the political freedom they had in mind here can be understood as negative liberty. In other words, both the neoliberal and the ordoliberal view can be understood as based on a consequentialist argument about how economic negative liberty is connected to political negative liberty. The neoliberals, however, simply made a quantitative claim, whereas the ordoliberals made a qualitative claim about what kind of economic liberty will maximize political negative liberty.<sup>29</sup> But unlike neoliberalism, the ordoliberal view can also be understood as invoking notions of positive liberty (indeed this is the only way to move from a quantitative understanding of negative liberty to a qualitative one), as incorporating a Hegel-like vision of the kind of civil society that they wanted to support, one in which the market was *free* in the competitive sense because this produced a society that was *just* regardless of the consequences for negative liberty. So while the ordoliberal view would arguably maximize negative liberty too even in the quantitative sense, this was beside the point: the point was to instantiate a vision of positive liberty. If ordoliberalism was to ensure that the market was free in the sense of *just*, some regulation and thereby some restraints on economic negative liberty would be required, regardless of whether this maximized negative liberty in the quantitative sense.<sup>30</sup> And the principle that ordoliberals used to operationalize their

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<sup>29</sup> Note that elsewhere I have argued the negative liberty cannot be maximized, only redistributed, an argument first put forth by Hillel Steiner. See, e.g., Hillel Steiner, *An Essay on Rights* (Oxford: Blackwell, 1994), pp 52-54. But regardless of whether negative liberty can be maximized, neoliberals (and no doubt most ordoliberals too) *think* it can be maximized, and here I am simply trying to explain their thinking, not address whether their reasoning is sound, so I will not address this issue any further here. Those interested in a full discussion of this issue, however, can find it in my *On Unemployment, Volume 1: A Micro-Theory of Economic Justice* (New York: Palgrave Macmillan, 2015) and *On Unemployment, Volume 2: Achieving Economic Justice after the Great Recession* (New York: Palgrave Macmillan, 2015).

<sup>30</sup> See, e.g., David J. Gerber, *Law and Competition in Twentieth Century Europe: Protecting Prometheus* (Oxford: Oxford University Press, 1998), pp. 232-265; David Gerber, "Two Models of Competition Law," in *Comparative Competition Law: Approaching an International System of Antitrust Law*, ed. Hanns Ullrich (Baden-Baden: Nomos-Verlagsgesellschaft, 1998), pp. 105-116, 112; Wernhard Möschel, "Competition Policy from an Ordo Point of View," in *German Neoliberals and the Social Market Economy*, ed. Alan Peacock and Hans Willgerodt (London: Macmillan, 1989), pp. 142-159.

conception of economic freedom was that of ensuring free competition, which entailed the idea that government regulation should be used to prevent activity likely to undermine this.<sup>31</sup>

In contrast, contemporary neoliberalism lacks such an operationalizing principle. Indeed, while the original neoliberals shared the ordoliberal conception of economic freedom, or at least shared their view of the types of economic regulation that would be permissible and the types that would not, contemporary neoliberals became side-tracked by their obsession with keeping the government out of their personal economic affairs and lost the thread of principle altogether. They ditched the idea of opposing only central planning and government-imposed price and production decisions and replaced it with the idea that *everything* government does is a form of impermissible interference. As Ronald Regan famously said to howls of appreciation, "government is not the solution to our problem; government *is* the problem."<sup>32</sup> This is not a principle, however, it is a slogan. It provides no coherent guidance as to why and therefore when government regulation should be opposed.

To see this, let us return to a moment to what seems to be a common neoliberal view that a market is the product of purely natural phenomena and therefore can exist completely independently of any outside regulatory authority. Even Robert Nozick, the most important contemporary intellectual to whom this particular view is typically attributed, did not actually believe this. He argued, of course, for what he called a minimal state,<sup>33</sup> but he never suggested that what we commonly conceive of as a market could exist if its potential participants were not able to enforce contracts, protect private property, and deter and punish

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<sup>31</sup> See, e.g., David J. Gerber, *Law and Competition in Twentieth Century Europe: Protecting Prometheus* (Oxford: Oxford University Press, 1998), pp. 232-265; David Gerber, "Two Models of Competition Law," in *Comparative Competition Law: Approaching an International System of Antitrust Law*, ed. Hanns Ullrich (Baden-Baden: Nomos-Verlagsgesellschaft, 1998), pp. 105-116, 112; Wernhard Möschel, "Competition Policy from an Ordo Point of View," in *German Neoliberals and the Social Market Economy*, ed. Alan Peacock and Hans Willgerodt (London: Macmillan, 1989), pp. 142-159.

<sup>32</sup> Steven R. Weisman, "Reagan Takes Oath as 40th President; Promises an Era of 'National Renewal' Minutes Later, 52 U.S. Hostages in Iran Fly to Freedom after 444-Day Ordeal," *The New York Times* (January 21, 1981).

<sup>33</sup> See Robert Nozick, *Anarchy, State, and Utopia* (New York: Basic Books, 1974).

theft and fraud.<sup>34</sup> And while Nozick did not say anything about whether the suppression of anti-competitive behavior would also be an acceptable activity of the minimal state, such a position is completely consistent with his view. He was, for example, very concerned with the idea of coercion,<sup>35</sup> and it seems clear that the reason anti-competitive behavior is objectionable is that it is in effect a form of economic blackmail. Indeed, even the most ardent neoliberals seem to agree that monopolization is coercive and therefore something that government should prevent given the free market baseline. Hayek, for example, who many see as the father of contemporary neoliberalism, expressly saw anti-competitive behavior as objectionable and therefore within the limited remit of what government could and should take action to prevent.<sup>36</sup> In any event, it is hard to see a "market" in which a single albeit private seller controls everything and therefore can set prices and make production decisions according to his own preferences without regard to the preferences of his customers as a "free" market in any meaningful sense. It is therefore hard to see how competition protecting legislation can be outside the scope of what the freedom protecting minimal state can do, if we accept that free markets are an essential component of political freedom.<sup>37</sup>

The problem, then, with using the idea of the minimal state as providing a principled way to sort acceptable rights protecting and market-enabling legislation from unacceptable government meddling is that while Nozick implied that a state that did "only" this would be minimal indeed, quite a lot of regulation can actually be placed in one of these categories. In fact, it is hard to think of a government regulation that cannot be described as aimed at the

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<sup>34</sup> See Robert Nozick, *Anarchy, State, and Utopia* (New York: Basic Books, 1974).

<sup>35</sup> See Robert Nozick, "Coercion," in *Socratic Puzzles* (Cambridge: Harvard University Press, 1997), pp.15-44.

<sup>36</sup> See F. A. Hayek, "The Meaning of Competition," and "'Free' Enterprise and Competitive Order," in *Individualism and Economic Order* (Chicago: University of Chicago Press, 1948), pp. 92-106 and 107-118. See also H. C. Simons, "A Positive Program for Laissez Faire," *Public Policy Pamphlet No.15* (Chicago: University of Chicago Press, 1934) (considered one of the founding documents of neoliberalism, although ultimately rejected by the second-generation neoliberals).

<sup>37</sup> There is also some controversy over whether libertarians can derive the prohibition of fraud from self-ownership, as Nozick claims they can do. See, e.g. James W. Child, "Can Libertarianism Sustain a Fraud Standard?" *Ethics* 104 (1994): 722-738. Child may indeed be right about this, but if one believes in economic freedom then one has to believe that the prohibition of fraud is legitimate. So while Child's point may raise a problem for libertarianism, it does not raise a problem for economic liberalism per se.

prevention of theft, fraud, or anti-competitive behavior, and certainly much of the legislation to which contemporary neoliberals currently object (such as the re-regulation of the financial industry) seems to fall squarely within one or more of these categories. In any event, unless one is going to embrace anarchism (and contemporary neoliberals would deny that this is what they are arguing we should embrace), it is hard to see any principled basis for objecting to all forms of governmental regulation no matter what its content. And while it is true that one often hears neoliberals say "that government is best which governs least," this is again a quantitative not a qualitative principle, and therefore cannot be taken seriously, for it would imply that a government that does not enforce contracts or protect private property is better than one that does, and those who use this slogan certainly don't believe that. What is required is some principle that allows us to evaluate government regulations according to their content, not their quantity, and if the ordoliberal principle of promoting and protecting competition is to be rejected for this purpose it is hard to see what principle or coherent set of principles neoliberals could possibly be using in its place. At least it is hard to see what other principle could be found in the idea of economic liberalism, whether of the Smithian or Hegelian sort, and so any other principle could not claim to be non-political in the way that principles based on economic liberalism claim to be non-political, that is, only in the slippery slope causal sense.

Even the slippery slope argument, however, does not hold up well when we subject it to reasonable scrutiny. I suppose we might consider it plausible to suggest that full-on central economic planning requires the kind of intrusive government institutions that could not help but want to manage all aspects of our lives, and this might accordingly support a consequentialist argument against central planning in the name of protecting negative political liberty. But the causal claim becomes distinctly implausible when used to suggest that *every* regulation of the market leads to this kind of intrusion. In other words, it is simply not clear that less regulation of the market no matter what kind of regulation we are taking about will actually increase individual negative liberty overall (economic and political) even in the

quantitative sense. One has more liberty if one can choose from a variety of suppliers who are all competing with each other; one has less if there is only one and therefore everyone has no choice but to deal with that sole supplier on whatever terms he may demand. Indeed, the notion that restricting certain kinds of freedoms can actually have the effect of increasing freedom overall is nothing new—both Kant and Hayek subscribed to it.<sup>38</sup> So even if we are talking about maximizing negative liberty in the quantitative sense, it is not clear that the neoliberal view adds up.

But there is another, more fundamental problem with the neoliberal position that all government regulation is freedom infringing in the negative liberty sense and therefore something to be opposed at all (or at least substantial) cost. Negative liberty was never intended to be a political concept. Rather, it was always intended to be an analytical concept, as a way a way of determining when a certain kind of freedom (the opportunity to act in ways in which we have the capacity to act without interference from other human agents) is infringed. It is an analytical and not a political concept because it does not tell us when such infringement is prohibited, permitted, or required and when it is not—some other theory of political morality is needed to do that. Negative liberty merely tells us when there has been an infringement, and thus when there is something that needs justification—it does not provide that justification nor suggest that no such justification is possible.<sup>39</sup> Indeed, almost everyone agrees that there are many infringements of negative liberty that are justified (the criminal law, for example, is full of them) and we would scoff at anyone who were to argue otherwise. If we do take negative liberty to be merely an analytical concept, however, we need some other principle to explain when regulation of the market and the infringements of negative

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<sup>38</sup> For discussions of Kant and Hayek's views on this matter, see Jeffrie G. Murphy, *Kant: The Philosophy of Right* (London: Macmillan, 1970), p. 92, and Chandran Kukathas, *Hayek and Modern Liberalism* (Oxford: Oxford University Press, 1989), pp. 142-143.

<sup>39</sup> See Isaiah Berlin, "Two Concepts of Liberty," in *Liberty*, ed. Henry Hardy (Oxford: Oxford University Press, 2002), pp. 166-217, pp. 172-173, 214-216.



liberty this entails is morally justified and when it is not, and by arguing that all forms of government regulation of the market are impermissible, contemporary neoliberalism simply fails to provide this.

Ordoliberalism, in contrast, does provide this. By this I mean it takes a much more plausible consequentialist position with regard to when increasing negative liberty will lead to greater negative liberty overall and when it will not, and offers the promoting competition principle as the way of instantiating this. And it also embodies a vision of positive liberty, a vision of a certain kind of society in which people should be able to live, the kind of society envisioned by Hegel, and therefore it is freedom promoting in the positive liberty sense as well. It is accordingly ordoliberalism that is protective of political freedom, whatever form of political freedom we embrace, whereas neoliberalism is not protective of political freedom at all, for it offers no conception of positive liberty and offers a conception of negative liberty that was intended as a measuring tool and not as an end in itself, and as an end in itself it is implausible and unattractive.

#### IV.

So how could economic liberalism split into two factions that are diametrically opposed to each other, yet each faction still believe that they are being true to the underlying convictions they both share? The genesis of this split can probably be traced to divisions arising between members of the Mont Pèlerin Society. Organized by Hayek in 1947, the Mont Pèlerin Society started out containing most of the economic liberals in the world, both Anglo-American and European, and the economic liberals of this period mostly saw themselves as the members of single group (and to some extent still do).<sup>40</sup> But as WWII receded and building a new Europe got underway, the European members of the Society discovered serious disagreements between them. Oddly enough, these disagreements tended to occur across national lines: the Austrians, by and large, advocated the kind of views we

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<sup>40</sup> For an extended discussion of the founding, make-up, an influence of the Mont Pèlerin Society, see *The Road from Mont Pelerin: The Making of the Neoliberal Thought Collective*, ed. Philip Mirowski and Dieter Plehwe (Cambridge: Harvard University Press, 2009), esp. ch.3: Ralf Ptak, "Neoliberalism in Germany, pp. 98-138.

now associate with neoliberalism, and the Germans the kind of views we now associate with ordoliberalism, although there were of course a range of views associated with each. The fact that both groups were German-speaking suggests that Hegel should be given more credit for having influenced their views than is commonly granted—after all, no self-respecting German-speaking intellectual then or now does not know their Hegel, but I'll get to this in a moment. A more pertinent fact for explaining the split may have been that the Germans and the Austrians were already on different sides of the *Methodenstreit*, the uncomfortably heated but seemingly pointless debate started by Carl Menger (on the Austrian side) and Gustav Schmoller (on the German side) over methods.<sup>41</sup> But the split between the neo and the *ordo* liberals seems to be more than simply a continuation of the *Methodenstreit*, for there really doesn't seem to be anything concerning method about it.<sup>42</sup> Rather, the most important factor seems to have arisen by historical accident. The Austrians mostly fled the rise of fascism and ended up in the United Kingdom and the United States, where fascism seemed an existential threat but not an internal one.<sup>43</sup> Their concern therefore naturally focused on socialism, which seemed the more credible ideological threat, the one that could arise within, as opposed to fascism, which threatened destruction by external sources. The Germans, in contrast, largely stayed behind and rode out the Nazis.<sup>44</sup> For them, the threat posed by fascism was naturally

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<sup>41</sup> The debate was over the extent to which economic research should be based on historical data and the extent it should be based on theory. See generally Clark Nardinelli and Roger E. Meiners, "Schmoller, the *Methodenstreit*, and the Development of Economic History," *Journal of Institutional and Theoretical Economics* 144 (1988): 542-551. Of course, any sensible economic claims should rely on both, and the claims made by both sides usually did. The debate was therefore largely over emphasis, a very murky question indeed.

<sup>42</sup> There is one sense in which the split between neoliberals and ordoliberals can be seen as a continuation of the *Methodenstreit*, although neither side seems to have viewed it as that: Following Menger, the Austrians were much more interested in theory than in facts. By this I mean that if theory predicts something, and it doesn't happen, this was just as likely to be viewed as caused by our misperception of reality than by mistake in the theory, whereas the Germans were much more amenable to revising their theories according to the evidence before them. Thus, neoliberals are convinced that adding to the money supply must cause inflation; and the fact that it hasn't does not show there is anything wrong with the theory. The fact that it must is viewed as a conceptual truth not amenable to challenge by empirical data.

<sup>43</sup> Whether this is why most of the American and British economic liberals tended to side with the Austrians, or why the Austrians tended to have different views than the Germans is unclear. To some extent, both kinds of influence were no doubt in play here.

<sup>44</sup> Even those that left Germany did not get very far—Wilhelm Roepke and Alexander Rüstow, for example, spent most of the War in Turkey (Roepke went to Switzerland toward the end of the War),

more salient than the threat posed by socialism. And with fascism, it was private power that seemed to be running amuck, not public power, or rather not only public power. Indeed, to the Germans the formation of large private business trusts and other anti-competitive combinations had seemed an essential instrument in the rise of the Nazi government, and the Germans therefore perceived this as the key threat that had to be addressed if a repeat of the subversion of their democratic institutions was to be prevented.<sup>45</sup> So while the Austrians became neoliberals and focused their attention on preventing what they feared was going to be a slide toward socialism in their adopted nations (as did many of their Anglo-American hosts although—and this is important to note—as followers of the Austrians and not so much as leaders of the neoliberal movement themselves), the Germans became ordoliberals and focused on the anti-competitive power of private trusts and the tendency of such trusts in their own nation to nurture fascism. Because the neoliberals feared socialism more than fascism, they were obsessed with the central planning advocated by socialist economies—the effort to control prices and output and allocate resources through government fiat rather than consumer demand—and the relation this seemed to have with the rise of anti-democratic and anti-liberal government. Because the ordoliberals saw private economic power as largely responsible for the rise of Hitler and the Nazi party, they saw private economic power and not just government power as presenting a grave threat to freedom. They feared fascism, not (or not merely) communism, while the neoliberals seemed willing to accept a little fascism as long as it kept the communists at bay.<sup>46</sup> And while the first generation of neoliberals did not oppose

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and therefore had a very different experience in exile than those who spent the War in the UK or USA. See Samuel Gregg, *Wilhelm Röpke's Political Economy* (Cheltenham: Edward Elgar, 2010), p. 77.

<sup>45</sup> I realize, of course, that many of the ordoliberals who remained in Germany during the War were not engaged in active resistance to the Nazi's, but rather were trying to sway the Nazi leadership toward ordoliberal thought. But while some ordoliberals were no doubt inappropriately accommodating to the Nazi's while the Nazi's were in power, they were not Nazi's themselves, and once the War was over even the most conservative ordoliberals were clearly intent on preventing anything like the Nazi regime from rising again. See Ptak, pp. 117-119. It was the neoliberals, not the ordoliberals, who exhibited authoritarian tendencies after the War. See Ptak, p. 119.

<sup>46</sup> Despite having lived through the Nazi era, for example, Hayek was always more sensitive to what he saw as the continuing threat of socialism than he was to the continuing threat of fascism. He embraced the distinction between totalitarianism and authoritarianism, seeing the latter as consistent with liberal democracy, even suggesting at one point that the military regime of General Pinochet in Chile fit the bill of a limited state. See Renato Cristi, *Carl Schmitt and Authoritarian Liberalism*

government programs that did not look like disguised methods of central planning (Hayek, for example, like Hegel, was in favor of aid to the unemployed),<sup>47</sup> the second generation of neoliberals became much more dogmatic, as is often the case with intellectual movements. Instead of recognizing that there were some kinds of government action that were permissible or even essential to ensure free markets, the neoliberal view ultimately became one in which all government action was seen as equally and necessarily a step toward socialism and therefore a threat to freedom. Contemporary neoliberals simply opposed all government regulation no matter what its purpose, and the absence of an ability to articulate the difference between market enabling legislation and market interference got solved by simply arguing that no distinction need be made—all government regulation was unequivocally and irredeemably bad.

Ordoliberalism, in contrast, remained true to its original roots, perhaps because ordoliberals actually got to instantiate their pro-competitive principles and the ideas associated with them and see them flourish as part of what became known as the West German "economic miracle,"<sup>48</sup> while neoliberals were mostly relegated to being voices in opposition in their English-speaking adopted nations during the post-War period, at least until the 1980s. Of course, promoting competition can sometimes be controversial—the antitrust casebooks are filled with cases where one side argues that a particular behavior encourages competition and the other argues that it undermines it, so this is not always a bright line test

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(Cardiff: University of Wales Press, 1998), pp. 146-168, esp. p. 168 n. 16 (quoting interview with Hayek on a visit to Pinochet in Chile); Karen Fischer, "The Influence of Neoliberals in Chile before, during, and after Pinochet," in *The Road from Mont Pelerin*, pp. 306-346, pp. 326-327.

<sup>47</sup> See Hayek, *The Road to Serfdom*, pp. 125-126; F. A. Hayek, "Economic Freedom and Representative Government," in *New Studies in Philosophy, Politics, Economics and the History of Ideas* (London: Routledge & Kegan Paul, 1978), pp. 105-118, 111. For a discussion of Hegel's view on unemployment, see Herzog, p. 55 ff.

<sup>48</sup> See generally Lawrence H. White, "Ordoliberalism and the German 'Wonder Economy'," in *The Clash of Economic Ideas* (Cambridge: Cambridge University Press, 2012), pp. 231-245. For more on ordoliberalism and its role in post-War (West) German thinking, see, e.g., Herbert Gersch, Karl-Heinz Paqué, and Holger Schmieding, *The Fading Miracle: Four Decades of Market Economy in Germany* (Cambridge: Cambridge University Press, 1992) pp. 26-36; Razeen Sally, "Ordoliberalism and the Social Market: Classical Political Economy from Germany," *New Political Economy* 1 (1996): 233-257; Liza Lovdahl Gormsen, *A Principled Approach to Abuse of Dominance in European Competition Law* (Cambridge: Cambridge University Press, 2010), pp. 39-48; Werner Bonefeld, "Freedom and the Strong State: On German Ordoliberalism," *New Political Economy* 17 (2012): 633-656.

that can be easily applied. But there is certainly far more meat on the bones of the idea of ordoliberalism than there currently is on the idea of neoliberalism, even though ordo principles can themselves also be misunderstood and abused (elsewhere I have argued that the current German government is misapplying ordo principles in justifying its obsession with austerity, but I won't go into that argument here).<sup>49</sup>

In any event, whether I have got the genealogy of the ideas that became neoliberalism and ordoliberalism correct matters, I suppose, only for historians: what matters for contemporary political economists is how different these two views became. And what matters even more is the way these ideas have been presented to the general public, for the high-horse that neoliberals claim to be riding is actually a lot shorter than they claim. They claim to be protecting freedom, and act as if anyone who disagrees with them is not, but what ordoliberalism shows is that economic liberalism and the freedom it can be understood to protect can be instantiated in very different ways. It was Hegel, not Smith, that actually supplied a substantive deontological argument for a connection between economic and political freedom and not merely a consequentialist one; and it was ordoliberalism not neoliberalism that provided a way of operationalizing this as well as a more plausible version of the consequentialist argument. And indeed the ordoliberal way seems much more principled and comprehensive, whereas the neoliberal way, at least as it has now come to be understood, seems to involve an abdication of principle for paranoia.

#### V.

The central organizing metaphors of Smith and Hegel—or rather what has come to be taken as their central organizing metaphors—can also be seen to encapsulate the difference in approach adopted respectively by ordo and neo liberalism. For Smith, this central metaphor is the idea of the invisible hand—the idea that uncoordinated actions of a large number of individuals can sometimes have a certain effect even though achieving that effect is neither intended or even desired by anyone involved. This wider effect, the saying goes, is

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<sup>49</sup> See my *On Unemployment: A Micro-Theory of Economic Justice* (forthcoming).

nevertheless achieved as if guided by an invisible hand. As applied to economic activity, neoliberals see this metaphor as standing for the proposition if that of one leaves the market alone it will be more efficient and therefore more productive (that is, create more total wealth, and therefore more wealth for everyone, at least potentially) than if one were to deliberately try to further this goal through market intervention. And in the politicized version of Smith's thought, neoliberals take the invisible hand metaphor to stand for the proposition that if we simply let people alone to pursue their own selfish interests, they will actually promote the common good far better than we could if we tried to promote this directly.<sup>50</sup>

What Smith meant by his use of this metaphor, however, and what contemporary neoliberals have taken him to have meant are very different. Smith used the term only twice in all his work; once in *A Theory of Moral Sentiments* ("TMS") and once in *The Wealth of Nations* ("WN").<sup>51</sup> In WN he said:

But the annual revenue of every society is always precisely equal to the exchangeable value of the whole annual produce of its industry, or rather is precisely the same thing with that exchangeable value. As every individual, therefore, endeavors as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to render the annual revenue of society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry he intends only his own security; and by directing that industry in such in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest, he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good. It is an affectation,

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<sup>50</sup> See generally Warren J. Samuels and Steven G. Medema, 'Freeing Smith from the 'Free Market': On the Misperception of Adam Smith on the Economic Role of Government,' *History of Political Economy* 37 (2005): 219-226; John F. Henry, "The Ideology of the Laissez Faire Program," *Journal of Economic Issues* 42 (2008): 209-224.

<sup>51</sup> Actually, he used the term three times, but the third was in an essay about astronomy, see Adam Smith, "The Principles Which Lead and Direct Philosophical Enquiries; Illustrated by the History of Astronomy," in *Essays on Philosophical Subjects* (Dublin 1795), sec. 3, p. 34, and its use there has no relevance to its use as a metaphor for the relation between selfish economic activity and the common good, so I will not discuss it further.

indeed, not very common among merchants, and very few words need to be employed in dissuading them from it.<sup>52</sup>

Note first where this comment actually appears: in a chapter called "Of Restraints Upon the Importation of Foreign Countries of Such Goods that Can Be Produced at Home." In other words, this chapter is an argument against enacting protectionist legislation such as the Corn Laws, which had done so much to hurt the poor, and an argument for the proposition that people will naturally prefer domestic produce to foreign produce without being forced to do so.<sup>53</sup> Exactly why people would actually do so when foreign produce is cheaper is not clear; indeed, the thrust of Smith's overall argument is that people will naturally buy the cheaper goods. So there is substantial reason to question Smith's reasoning here.

But never mind that for the moment. Let us first take note of some other aspects of this passage. First, what Smith argues is that by pursuing their own self-interest people may indeed promote a public goal. But he makes no claim that this method of promoting public goals is *better* than any other method available. Indeed, all he suggests that it is not "always worse" for society that the individual does not intend to promote a public goal, which is a far cry from saying it is always better. And he makes no comparison between a world where everyone pursues their own interests and one where the government intervenes in the market in an attempt to promote some public good. The comparison he actually makes is between a world where everyone pursues his own interest and one where some private individuals try to promote the public good, and suggests that the efforts of the few in that latter world are most likely to be ineffectual. This is actually an argument *for* government intervention in the marketplace, not an argument against it, for it suggests that the coordinating properties of government action are necessary in these circumstances because we cannot rely on the uncoordinated private action of the altruistic few. So to the extent contemporary neoliberal

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<sup>52</sup> Adam Smith, *The Wealth of Nations* (New York: Modern Library ed. 2000), bk. 4, ch.2, pp. 485-486.

<sup>53</sup> See also Smith, *The Wealth of Nations*, at p. 488, 560 ff.

claim that non-interference is the best policy, that claim has no basis in this passage from Adam Smith.<sup>54</sup>

Even if we take Smith to have intended to make a larger claim about the invisible hand and suggested that it could indeed promote the public good better than the visible hand of government, however, we have no reason to think he meant this claim to apply in all cases. As George Osborne, who is now Chancellor of the Exchequer for the current conservative-led UK government and a supposed fan of free markets, said in the introduction to a recent edition of WN:

Of course, Adam Smith was no utopian. He was keenly aware of the limitations of the “invisible hand” – and therefore understood that effective institutional infrastructure is required to ensure the operation of a free and fair market. Unfettered markets tended toward monopolization, he wrote, and so proportionate government action is needed to create a clear and stable framework that enables free competition to take place. Getting that balance right remains as important in the age of software giants as it was in the age of cotton kings.<sup>55</sup>

In other words, markets do not exist in a vacuum. They must be established by rules that enforce contracts, protect private property, prevent fraud and theft and anti-competitive behavior. Only within that context might it be better to leave the market unfettered. Suggesting that the market should be unfettered full stop is simply incoherent, because unless it is subject to a certain set of rules, the market—at least the market that we know today and that Smith and Hegel took as being a social institution worth improving—could not even exist.

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<sup>54</sup> To be fair, I should acknowledge that there are various other points in WN where Smith's comments do sound like an endorsement of *laissez faire*. But there are just as many other points where Smith's comments endorse government intervention. In any event, I have already addressed which view is the better characterization of Smith's work taken as a whole. My purpose here, however, is far more limited: simply to take a closer look at what Smith said about the “invisible hand.” For a more extensive discussion of this issue, see William Grampp, “What Did Smith Mean by the Invisible Hand?” *Journal of Political Economy* 108 (2000): 441-465.

<sup>55</sup> George Osborne, MP, “Forward,” WN (Harriman House, 2007), forward by George Osborne MP. See also Herzog, *Inventing the Market*, pp. 99, 124 for proposition that Smith rejected idea that selfishness in the marketplace necessarily leads to the common good.



But let us look at the other mention of the invisible hand to see if that supports the neoliberal position. In TMS Smith says

It is to no purpose, that the proud and unfeeling landlord views his extensive fields, and without a thought for the wants of his brethren, in imagination consumes himself the whole harvest that grows upon them. The homely and vulgar proverb, that they eye is larger than the belly, never was more fully verified than with regard to him. The capacity of his stomach bears no proportion to the immensity of his desires, and will receive no more than the meanest peasant. The rest he is obliged to distribute among those who prepare, in the nicest manner, that little which he himself makes use of, among those who fit up the palace in which this little is to be consumed, among those who provide and keep in order all the different baubles and trinkets, which are employed in the economy of greatness; all of whom thus derive from his luxury and caprices, that share of the necessaries of life, which they would have in vain expected from his humanity and greatness. The rich only select from the heap what is most precious and agreeable. They consume little more than the poor, and in spite of their natural selfishness and rapacity, though they mean only their own conveniency, though the sole end which they propose from the labours of all the thousands whom they employ, be the gratification of their own vain and insatiable desires, they divide with the poor the produce of all their improvements. They are led by an invisible hand to make nearly the same distribution of the necessaries of life, which would have been made, had the earth been divided into equal portions among all its inhabitants, and thus without intending it, without knowing it, advance the interests of the society, and afford means to the multiplication of the species.<sup>56</sup>

First and foremost, notice that this is a distributional claim: Smith suggests that even though the landlord intends satisfaction only of his own selfish desires, he must still feed those who work for him as well as those who sell him luxuries if he is to live the kind of life that the current level of technology in his society makes possible. This, I suppose, is true; as Marx noted, there can be no labor if the laborer does not exist and the laborer cannot exist unless he (or she) is provided with enough wherewithal for his (or her) subsistence. But providing the laborer and the trinket-maker with the means of their subsistence is a far cry from dividing the spoils of production the landlord receives with everyone "as if the world had been divided into equal portions among all its inhabitants." That claim, to the extent this

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<sup>56</sup> Adam Smith, *The Theory of Moral Sentiments* (Cambridge: Cambridge University Press, 2002), pt 4, ch. 1, pp. 215-216.

is what Smith was actually asserting, is nonsense. If we were in any doubt about this, the recent fact that almost all gains in the economy have gone to those in the top 1 percent should quiet any of those who might still harbor such a delusion.<sup>57</sup> There is no invisible hand driving equal division of natural resources; at most there is an invisible hand driving those with everything to provide subsistence to a certain number of those who would otherwise starve, and while this is something it is not very much. It certainly does not amount to a claim that the invisible hand distributes the spoils of production just as they would be divided if everyone owned an equal share of the world's resources.<sup>58</sup> Moreover, it says nothing about the unemployed, or those who are not able to make trinkets that the wealthy want or work in their fields and therefore be provided with subsistence. These people—the ones whose existence is unnecessary to the maintenance of the lifestyle that the rich are currently able to achieve—will starve. At least there is no causal mechanism set forth by Smith to explain why the rich might provide for these individuals' subsistence. Even with regard to those whose continued existence is necessary for the maintenance of the lifestyle of the rich, there is no

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<sup>57</sup> On this point see, e.g., Estelle Sommeiller and Mark Price, "The Increasingly Unequal States of America: Income Inequality by State, 1917 to 2012," *Economic Analysis and Research Network Report* (January 26, 2015), p. 5 (available at <http://s3.epi.org/files/2014/IncreasinglyUnequalStatesofAmerica1917to2012.pdf>); Lawrence Mishel and Nicholas Finio, "Earnings of the Top 1.0 Percent Rebound Strongly in the Recovery," *Economic Policy Institute Issue Brief #347* (January 23, 2013); Edward N. Wolff, "The Asset Price Meltdown and the Wealth of the Middle Class," NBER Working Paper Series, Working Paper 18559 (National Bureau of Economic Research, November 2012).

<sup>58</sup> I note that Smith claims only that "necessaries" will be distributed as if the resources that produced them were owned equally by everyone. The term "necessaries" has a very specific meaning within English and also Anglo-American common law—it refers to things like food, clothing, and shelter that are essential for basic subsistence. See, e.g., Frederick Stroud, *The Judicial Dictionary of Words and Phrases Judicially Interpreted, Volume 2*, (London: Sweet and Maxwell, 2d ed. 1903), pp. 1249-50; P. H. Winfield, "Necessaries Under the Sale of Goods Act, 1893," *Law Quarterly Review* 58 (1942): 82-95. Given that Smith was a lawyer, one might think that this restrictive meaning is what he intended. But Smith is using the term in a more expansive way—he is not limiting it to what we might call *primary* basic needs, but including goods that constitute *contextual* basic needs as well. See Smith, *Wealth of Nations*, bk. 5, ch. 2, pt. 2, pp. 938-939. That is, he is including not only goods strictly necessary for survival, but also goods that are necessary for individuals to feel like they are fully accepted members of society, given the level of welfare in the culture in the time and place they live and perhaps their social class. (For more on how the distinction between primary and contextual basic needs might be cashed out, see my *Exploitation and Economic Justice in the Liberal Capitalist State*, pp. 127-136.) But even if the more narrow reading of the term is what is appropriate here, Smith's claim is not correct, for the amount of necessaries that are required for subsistence is far less than the amount that would satiate most people, and therefore even with regard to these primary basic goods, it is not likely that the rich are going to pay the poor enough so that both the rich and the poor end up with the same amount they would if the world's resources were equally divided.

causal explanation of why the rich would pay *a just price* for the labor of the poor, and not merely bare subsistence.<sup>59</sup> Once again, without some sort of government intervention—without the very *visible* hand of some sort of collective moral power—this is unlikely to occur. So to the extent that Smith is making a claim about the invisible hand here, it is a modest claim indeed. At most, Smith is saying that by pursuing their own interests the rich also advance to some extent the interests of society, not that they advance the interests of society to a greater extent than if their admittedly naturally self-centered and avaricious behavior were moderated in some way by government regulation and their activities taxed and the proceeds redistributed to some extent to instantiate a more all-encompassing vision of the common good. So what Smith actually said is nothing like the claim that neoliberals attribute to him, to the effect that the invisible hand will produce the common good better than if government intervened and tried to do this itself.

Finally, it is important to put Smith's remarks in their proper context. First, remember that Smith was railing against the suffocating interference of protectionism and the guild system, not advocating that the market be totally unfettered. But more importantly, remember that at the time Smith was writing, a substantial body of philosophical and religious opinion going back more than a thousand years argued that profit-seeking in economic transactions was morally wrong.<sup>60</sup> Smith was part of a long slow trend that went from condemning economic egoism as a moral motive to one that was trying to make the pursuit of profit morally acceptable.<sup>61</sup> Yet the contemporary neoliberal interpretation of his views goes way beyond this—instead of merely arguing that the pursuit of economic self-interest is not necessarily morally objectionable, the contemporary neoliberal view is that it is always morally acceptable and, even more strongly, morally *optimal*. What Smith argued for was

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<sup>59</sup> For my conception of the just price, see Reiff, *Exploitation and Economic Justice in the Liberal Capitalist State*.

<sup>60</sup> For further discussion of the evolution of these views, see my *Exploitation and Economic Justice in the Liberal Capitalist State*.

<sup>61</sup> See Albert O. Hirschman, *The Passions and the Interests* (Princeton: Princeton University Press, 1977).

that good can come out of economic egoism—he did not argue that pursuing economic egoism was the equivalent of pursuing the common good. Indeed, had Smith been arguing that nothing was needed to reign in the excesses of greed, as contemporary neoliberals contend, then that would have made him an economic radical, not a liberal, for it would have represented a shift from one extreme to the other rather than a mere attempt at liberalization of the prevailing moral attitude toward economic egoism. So the central metaphor on which neoliberals rely is really a rather large departure from Smith's actual views. It is ordoliberalism, not neoliberalism, which represents a more faithful instantiation of his views.

Ordoliberalism is also a more faithful instantiation of Hegel's views, and it does seem that given the German-speaking origins of many of the most important neo and ordo liberals we should pay more attention to Hegel's views on the market than we typically do in the English-speaking world. Of course Hegel also recognized something like the invisible hand—the idea that sometimes something completely unintended can be accomplished by aiming at something else. Hegel called this "the cunning of reason."<sup>62</sup> But this idea is not the central defining metaphor of his work. Instead, the central defining metaphor for Hegel's view of the market is the civil society, and Hegel said a lot more about the civil society than Smith ever said about the invisible hand.<sup>63</sup> While the exact scope of what Hegel meant by the civil society remains somewhat open to debate and the metaphor can accordingly be interpreted in different ways by those on different sides of the political spectrum,<sup>64</sup> the most persuasive interpretation of what Hegel meant is the interpretation most consistent with ordoliberalism. For example:

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<sup>62</sup> See generally, Charles Taylor, *Hegel* (Cambridge: Cambridge University Press, 195), p. 74. For interesting and helpful comparisons between these two concepts, see Edna Ullman-Margalit, "The Invisible Hand and the Cunning of Reason," *Social Research* 64 (1997): 181-198; H. B. Acton, "Distributive Justice, The Invisible Hand and the Cunning of Reason," *Political Studies* 20 (1972): 421-431.

<sup>63</sup> See, e.g., G. W. F. Hegel, *Elements of the Philosophy of Right* (Cambridge: Cambridge University Press, 1991), §§182-256. For a helpful discussion of Hegel's discussion of the civil society, see the introduction to that volume by Allen Wood, pp. xvii-xxvii.

<sup>64</sup> For a discussion of the ways in which Hegel can be taken to have been a liberal and the ways in which he can be taken to have been a conservative, see Charles Taylor, *Hegel*, pp. 449-461.

Hegel discusses the market as part of 'civil society,' which he characterizes as an association of members as self-subsistent individuals in a universality which, because of their self-subsistence is not abstract . . . For Hegel civil society includes the 'system of needs,' the 'administration of justice,' and the 'police and corporations;' it can thus be described as the market economy together with the institutions that make it possible and that grew out of it.<sup>65</sup>

But

Hegel's market is not the peaceful, self-adjusting mechanism that Smith had described. If one zooms in from the macroeconomic to the microeconomic level, as it were, one realizes that the market is a battlefield of everyone against everyone else—and hence the 'relic of the state of nature'—and of each against the common interests of the community.<sup>66</sup>

Indeed,

given how problematic the market is for Hegel, it is not surprising that he puts a stronger focus than Smith on the institutions that limit and correct market outcomes, introducing additional elements of 'universality' into the sphere of civil society.<sup>67</sup>

Thus, for Hegel, it is civil society and its institutions that provide a framework within which "free" market activity can take place. Without that framework, there can be no market, much less a free one, for there would be no way to protect the individual rights of the participants nor ensure that the market was furthering the common interests of the community.

Now I do not contend that Hegel should be seen as just as influential a voice as Smith when it comes to defining economic liberalism. Even within the German-speaking world, Hegel is not often explicitly discussed by those who consider themselves economists, with the very important exception of Marx and his followers, who are obviously heavily influenced by Hegel's work. But Hegel was enormously influential on German intellectual thought in a

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<sup>65</sup> Herzog, at p. 53. Note that this also makes Hegel an important (albeit largely unnoticed) antecedent of "institutionalist economics"—the name given to the work of people like Thorstein Veblen, Wesley Mitchell, and John R. Commons, who argued that the market cannot be separated from the political and social system in which it is embedded. The institutionalists could be viewed as American ordoliberalists, see Schnyder and Siems, "The Ordoliberal Variety of Neoliberalism," but I will not have time to go into that connection here. For more on institutional economics in general, however, see Geoffrey M. Hodgson, "What is the Essence of Institutional Economics?" in *The Philosophy of Economics*, ed. Daniel M. Hausman (Cambridge: Cambridge University Press, 3rd ed. 2008), pp. 399-412; Gunnar Myrdal, "Institutional Economics," *Journal of Economic Issues* 12 (1978): 771-783; John R. Commons, "Institutional Economics," *American Economic Review* 21 (1931): 648-657.

<sup>66</sup> Herzog, at p. 54 (footnote omitted).

<sup>67</sup> Herzog, at p. 56.

more general way, and his work was certainly part of the *Zeitgeist* that all German-speaking economists grew up within, as Joseph Schumpeter himself remarks in his massive *History of Economic Analysis*.<sup>68</sup> In other words, German-speaking intellectuals were effectively infused with Hegel's work because of its importance within German-speaking culture—it became part of the way these people *thought*, whether they were expressly discussing Hegel or not, and therefore his ideas cannot help but lie underneath much of what post-Hegelian German economic liberals were saying, especially the ones who continued writing in German as the ordoliberals did. And while I do not contend that Hegel's conception of the civil society can be cashed out in any definitive way through a close inspection of Hegel's use of the term, this is not the point. The point is that the central defining metaphor of his work (as far as his work relates to political economy) does a much better job of capturing what Smith actually meant in his work and therefore what economic liberalism originally embodied. Indeed, it is no mere coincidence, I submit, that one of the leading works by Wilhelm Roepke, an important ordoliberal, is called *The Moral Foundations of Civil Society*.<sup>69</sup> And while Roepke does not expressly tie his use of the term "civil society" to Hegel's, he was certainly aware of the role it played in Hegel's work and it is therefore reasonable to assume that Roepke was in some sense echoing, at least unconsciously, this important aspect of Hegel's thought.

Indeed, in their own ways, both the original neoliberals and the original ordoliberals no doubt saw themselves as working toward creation of the civil society, even though contemporary neoliberals clearly do not. So as far as being true to the founding notions of economic liberalism is concerned, the metaphor of the civil society seems much more apt than that of invisible hand. An invisible hand is a parlor trick; the civil society is an objective. A civil society is something we can work toward; simply allowing ourselves to be pushed along by the invisible hand is a way of abdicating any conscious attempt to achieve a political objective and leaving our fate to the outcome of whatever complex causal processes may be

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<sup>68</sup> See Joseph A. Schumpeter, *History of Economic Analysis* (Oxford: Oxford University Press, 1954), p. 413.

<sup>69</sup> See Wilhelm Roepke, *The Moral Foundations of Civil Society* (New Brunswick, Transaction Publishers, 1948, 1966).

currently in play, admitting that these are processes are something we can never fully identify much less understand or influence or control. Accordingly, claiming that we should simply leave ourselves in the palm of the invisible hand sounds like claiming we should leave the organization and maintenance of society to some mysterious power behind the scenes. But given its rejection of the idea that there is a social and economic order mandated by God or at least not subject to human control, this is an idea that should sound antithetical to those who embrace the tenets of political liberalism. And since economic liberalism is supposed to ensure the protection of political liberalism (and by political liberalism I mean liberalism in its general enlightenment sense and not in the sense of a collection of leftish political concerns),<sup>70</sup> it seems like the contemporary idea of the invisible hand is something about which we should be very wary indeed. The all encompassing metaphor of the civil society, in contrast, is much more in tune with economic liberalism and therefore political liberalism than the rather narrow and constraining metaphor of the invisible hand. Indeed, if we delude ourselves into thinking otherwise, we risk waking up one day to find ourselves staring at an invisible hand that is raising itself in a fascist salute.

## VI.

I want to close by making some remarks intended to ensure that the claims I am making in this paper are kept in their proper context. This paper is not intended as a general defense of ordoliberalism, or even as an argument that ordoliberalism represents the best possible interpretation of the economic liberalism of Smith or Hegel. It is simply intended to point out that as between contemporary ordoliberalism and neoliberalism, ordoliberalism is both more consistent with economic liberalism and offers more potential resources for dealing with contemporary economic problems. But of course there are a range of views that can be described as ordoliberal, some are more attractive than others, ordoliberals can disagree on how best to instantiate their views, and like their neoliberal siblings, some contemporary

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<sup>70</sup> For more on how my use of the term "political liberalism" should be understood, see my *Exploitation and Economic Justice in the Liberal Capitalist State*, pp. 18-24.

ordoliberals seem to be straying pretty far from we might think of as their core beliefs.<sup>71</sup> But further discussion of ordoliberalism's many and sundry nuances is not possible here. What I have been trying to do in this paper is simply suggest that acquainting ourselves better with ordoliberal thinking gives us an opportunity to understand economic liberalism in new ways. And armed with this better understanding, I hope those who consider themselves economic liberals can now see that there is an alternative way forward, one that is very different and potentially much more productive than the way forward neoliberalism currently presents.<sup>72</sup>

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<sup>71</sup> For a discussion of this with regard to ordoliberal (in my view misguided) support for austerity as a way to combat unemployment and recession, see Reiff, *On Unemployment, Volume I: A Micro-Theory of Economic Justice*, pp. 128-134.

<sup>72</sup> Earlier versions of this paper were prepared for a symposium on Lisa Herzog's *Inventing the Market*. My thanks to Lisa Herzog for inspiring this paper, and for her very helpful comments and suggestions on earlier drafts.