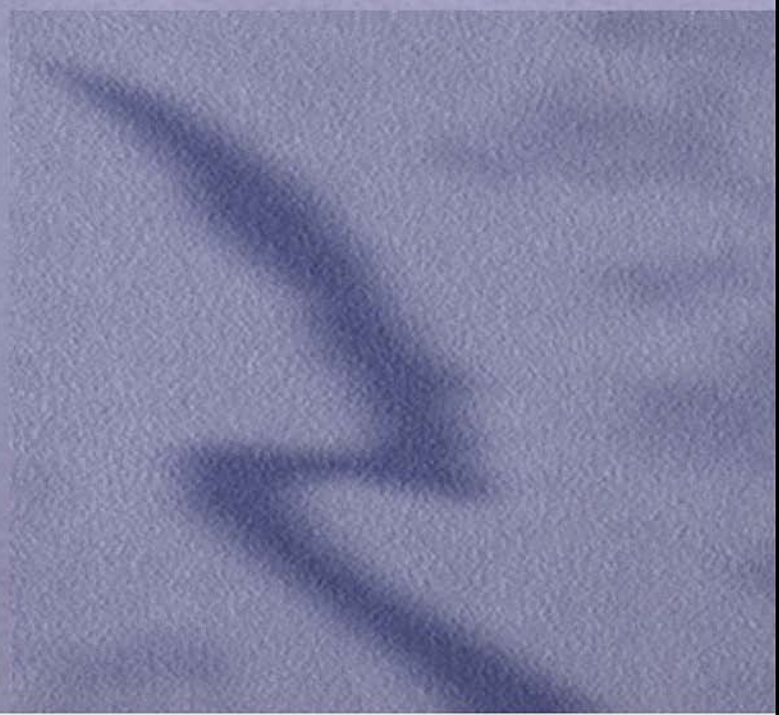
The German Historical School

The historical and ethical approach to economics

Edited by Yuichi Shionoya

Routledge Studies in the History of Economics



The German Historical School

The German Historical School of Economics, which exerted a strong influence on the German-speaking world throughout the nineteenth century, was a reaction to rationalism and enlightenment and challenged the British classical economics. It also attacked neoclassical economics and Marxian economics which were emerging descendants of the classical economists. The Historical School was characterized by its emphasis on historical and ethical methods, and just for this reason it has been misunderstood by mainstream economics as an unscientific standpoint. However, with the inceasing acceptance of evolutionary and institutional thinking among economists, general interest in the German Historical School has risen steadily during the past decade.

This book clarifies the approach of the German Historical School by the reconstruction of their achievements in terms of rational and historical context. To trace the development and transformation of their ideas, this book covers not only the leading figures of the school such as Adam Müller, Wilhelm Roscher, Karl Knies, Lujo Brentano, Gustav von Schmoller, and Werner Sombart, but also those who have proved to be closely related to the thought of the Historical School in different ways, such as Carl Menger, Anton Menger, Friedrich von Wieser, Max Weber, Joseph Schumpeter, Tokuzo Fukuda, Walter Eucken, Wilhelm Röpke, and Alfred Müller-Armack.

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Introduction

Yuichi Shionoya

With the increasing acceptance of evolutionary and institutional thinking among economists, general interest in the German Historical School has risen steadily during the past decade. The Historical School was a reaction to rationalism and the Enlightenment and challenged British classical economics, which had allegedly presented a universally valid economic theory. It also criticized neoclassical economics and Marxian economics as descendants of classical economics. The Historical School is characterized by its emphasis on historical and ethical methods, and just for this reason it has long been misunderstood, mainly by mainstream economists, as an unscientific approach that would oppose theoretical formulation and advocate value judgments.

To be understood, the German Historical School needs to be reconstructed within a historical and rational context. In fact, it was oriented toward the industrialization of less developed Germany and concerned with building an institutional framework in which ethics was embedded. But the importance of the school is not confined to its historical role alone. A new perspective for economics will be suggested through an interpretation of the German Historical School that provides an alternative to present-day mainstream economics with regard to scope and method.

This book intends to clarify the historical and ethical approach that was developed by the old, younger, and youngest Historical School and to trace the transformation of ideas not only in Germany but also in other countries. The major concepts developed by the German Historical School are identified as institution, evolution, and national policy, and historical and ethical methods were required to explore these key concepts. Thus recent thought in economic and social theory such as institutionalism, evolutionism, and communitarianism can be conceived to have originated in the Historical School and related schools of thought.

This volume is incidentally characterized by the contributions of Japanese authors. In the latter half of the nineteenth century, after the opening of the country to the modern international world, Japan rapidly introduced social institutions, ideologies, sciences, and technologies from Western

countries including Great Britain, Germany, France, and the United States. In the crucial period of nationbuilding, Japan modelled its Constitution and prominent government institutions on those of Germany. In founding the first national university (Tokyo Imperial University), which naturally enjoyed privilege and influence, the government adopted the German education system. As a result, Japanese academe in economics established a special relationship with its German counterpart, although it did not exclude the influences of other advanced countries (classical economics, neoclassical economics, and Marxian economics). The dominant economics in Germany at that time was that of the Historical School; its economics of state intervention and social policy appealed greatly to Japanese intellectuals. For over a century since then, Japanese economists have maintained an active interest in the development of economic thought in Germany— for instance, inviting visiting professors from Germany, including Emile Lederer and Alfred Amon, to Tokyo Imperial University (Joseph Schumpeter almost accepted a post there just before settling in Bonn), sending young scholars to German universities, and translating contemporary and classical German books on economics.

This tradition has survived the temporary decline of German economics in the aftermath of World War II. Unlike present-day German economists who hesitate to deal with economic, social, and political thought under the Third Reich, Japanese scholars may be less handicapped and more cool-headed in their appraisal of the German Historical School, whatever influences it is alleged to have exerted on Nazi ideology. Thus we have the pleasure of presenting such a contribution to the study of German economic thought to fill the unhappy lacuna.

This volume is neither a textbook nor a comprehensive anthology of the German Historical School. It is based in part on the papers submitted to a plenary session on the Historical School organized at the annual meeting of the Society for the History of Economic Thought (Japan) held in Tokyo in November 1996. In that this volume is edited with the support of that Society, it is a sequel to a volume by Shiro Sugihara and Toshihiro Tanaka (eds), *Economic Thought and Modernization in Japan* (Edward Elgar, 1998).

To trace the development and transformation of the ideas of the Historical School, this book covers not only the leading figures of the school such as Adam Müller, Wilhelm Roscher, Karl Knies, Lujo Brentano, Gustav von Schmoller, and Werner Sombart, but also those who have proved to be closely related to the thought of the school in different ways such as Carl Menger, Anton Menger, Friedrich von Wieser, Max Weber, Joseph Schumpeter, Tokuzo Fukuda, Walter Eucken, Wilhelm Röpke, and Alfred Müller-Armack.

In chapter 1, Yuichi Shionoya proposes a rational reconstruction of the German Historical School on the basis of the research program that Gustav von Schmoller advocated for the school. This chapter is intended to give

an overview of the economics of the Historical School and an introduction to the following chapters devoted to the historical reconstruction of individual scholars' achievements in the school. Referring to Joseph Schumpeter, Shionoya defines the research program of the Historical School as an attempt to integrate theory and history by means of economic sociology. He proposes to interpret the school's historical and ethical method on the basis of methodological holism and instrumentalism and demonstrates the relevance of its thought and method to institutionalism, evolutionism, and communitarianism.

In chapter 2, Tetsushi Harada focuses on Adam Müller, one of the forerunners of the German Historical School. In a survey of German economic thought, Wilhelm Roscher once argued that Müller's thought was half-historical or incompletely historical, because although Müller advocated the unique development of a nation based on its identity, he was skeptical about the spread of modern commerce and industry and hesitated to judge the development or underdevelopment of a nation according to its degree of commercialization. Harada pays special attention to Müller's work 'Agronomische Briefe' [Agronomic Letters], which reveals his characteristic position in this regard. In examining this material, Harada argues that Müller's proposal that Germany without the preconditions of industrialization and commercialization should keep 'isolated agriculture' to reduce the evils of commercialization rather than to promote 'commercial agriculture' is contrasted with that of Friedrich List, who advocated industrialization and commercialization by a means of the protection and corresponding expansion of agriculture.

Yukihiro Ikeda in chapter 3 introduces Wilhelm Roscher's lecture note, used in his early period at the University of Leipzig and now housed in the Library of Keio University. This document, which is thought to have been prepared between 1849 and 1851, is placed at the midpoint between his volumes *Grundriss zu Vorlesungen über die Staatswirtschaft* (1843) and *Die Grundlagen der Nationalökonomie* (1854). Ikeda is interested in this notebook not only to observe the development of Roscher's thought but also to investigate the method of university education at the time.

Chapter 4 on Karl Knies by Jun Kobayashi explores the methodological roles of Knies's concepts of *Analogie* and *Sitte* in the German Historical School. Kobayashi demonstrates that Knies's concept of analogy admits but limits the effectiveness of theory to specific stages in the development of society. Thus Knies suggested economic sociology or a theoretical approach to history through the concept formation of type which relies on the rhetoric of analogy. Then, Kobayashi argues that Knies defined economics as a science of man based on the concept of *Sitte* [ethics], which is endowed with the dual meanings of 'is' and 'ought', in contrast to the concept of economic man in the British Classical School. With regard to Wilhelm Hennis's argument that asserts a continuity between Knies and Max Weber

on account of a science of man, Kobayashi criticizes Hennis for neglecting Weber's dissociation from the German Historical School, which included normative elements as an essential part of its economics.

Sachio Kaku's essay in chapter 5 discusses Lujo Brentano's critique of the social insurance that was going to be introduced in Germany in the 1880s. Brentano worried that social insurance would conflict with the freedom of labor and so advocated the development of the labor union to fulfill the functions of social insurance rather than the interference of the state. Thus Kaku indicates the difference between Brentano and Schmoller in the *Verein für Sozialpolitik* in that Brentano's view was based on the belief in the market mechanism and the role of the labor union.

In chapter 6, Kiichiro Yagi pays attention to an aspect of the *Methodenstreit* that was concerned with conflicting views on the historical development of institutions. Carl Menger criticized Gustav von Schmoller for neglecting the spontaneous growth of institutions that was not based on the social will and the compulsory practice of the state. Although Schmoller did not join the discussion, Yagi interprets the legal theory of Anton Menger, the brother of Carl and a social reformer, as a relevant reply, which expanded the scope of the issue. Anton argued that even the legal order established through customs is in fact based on power relationships in society. Yagi then brings into the picture Friedrich von Wieser, the successor to Carl at the University of Vienna, and formulates the Austrian view of history based on Wieser's sociology of power as anonymous history drawn by the masses.

Shin'ichi Tamura in chapter 7 compares the views of Schmoller and Werner Sombart, the representatives of the younger and the youngest German Historical School, respectively, with regard to scientific method and policy proposals. Schmoller, based on the historical-ethical method, thought that the social policy would encourage the development of enterprise (particularly small enterprise) and the national economy through moral development. On the contrary, Sombart distinguished categorically between handicrafts and capitalism and tried to remove ethics from the notion of economic development, because, for him, capitalist development meant natural, non-personal development driven by the capitalist spirit. However, Sombart noticed a cultural crisis of capitalism that was brought about by material abundance and the mass society, so he finally presented the vision of falling capitalism and the recovery of agrarian society in the vein of premodern Romanticism.

In chapter 8, Kazuhiko Sumiya, the distinguished Weberian, presents his interpretation of the relationship between the German Historical School and Max Weber, which he characterizes as critical succession. He first summarizes the points entailed by massive literature on the work of Weber in the postwar period, focusing on how Weber inherited the legacy of the German Historical School, and then throws light on the relationships

between 'Die Agrarverhältnisse im Altertum', 'Die Psychophysik der Industriearbeit', and the series of *Grundriss der Sozialökonomik* edited by Weber to demonstrate that the vision of social economics resulted from his lectures on economics at Heidelberg and proved the critical succession of the German Historical School.

Although Joseph Schumpeter is not regarded as a member of the German Historical School, his methodological and substantive adherence to Schmoller is well known from his 1926 article on Schmoller. In chapter 9, Yuichi Shionoya discusses the development of the legacy of the German Historical School by Schumpeter, whose leitmotif was a comprehensive sociology and *Soziologizierung* of the social sciences. From this perspective Shionoya argues that Schumpeter was concerned about the relationship between economics and sociology; in his study on the history of economics, Schumpeter took seriously previous attempts to construct a grand theory or a universal science. Shionoya elaborates Schumpeter's structure of thought by analyzing his views on Auguste Comte, Karl Marx, Vilfredo Pareto, and Max Weber, among others, with regard to the relationship between economics and sociology.

Chapter 10, by Tamotsu Nishizawa, discusses the reception and transformation of economic thought of the German Historical School in Japan, focusing on Tokuzo Fukuda, the leading economist in the early decades of the twentieth century. When Fukuda studied in Germany, he published a book, *Labor Economics,* with his teacher Lujo Brentano which incorporated the social policy advocated by the German Historical School. He then shifted his interest to the welfare economics of Alfred Marshall and A.C.Pigou, which was more theory-oriented than German historical economics. Nevertheless, having been inspired by the social policy tradition of the German Historical School, he was not satisfied with the price economics of the Cambridge School and emphasized the development of the labor movement as a means of increasing welfare through the acquisition of satisfactory labor income based on the principle of need.

Before and after World War I discussion of the development and transformation of capitalism in Germany reflected the ideas of not only the German Historical School but also its critics. Osamu Yanagisawa in chapter 11 addresses how German economic thought affected Japan's view on the state regulation of the economy before World War II. In the 1930s, when Japan was at war with China, the government assumed control of the economy and economists were asked to offer theories for regulating it. Among the German economists, the most influential in Japan was Werner Sombart, who published *Zukunft des Kapitalismus* (1932) besides many other scholarly works. In that book he predicted a structural change in capitalism from the market mechanism to a planned economy; his idea provided a foundation for discussion in Japan. Yanagisawa also describes other behavior of Japanese economists in the prewar period that was

influenced by German economic thought: right-wing nationalism and an escape into the study of the history of economic thought.

In chapter 12 Naoshi Yamawaki considers the ordoliberalism represented by Walter Eucken and Wilhelm Röpke in terms of what they would accept and reject in the legacy of the German Historical School. He argues that they share with the Historical School the vision that theory is inseparable from history and policy. Eucken's morphological approach to the economic system, proposed in place of the stage theory of economic development that the Historical School was seriously concerned with on the presupposition of progressivism, led to the 'order policy' for the market system. Röpke tried to formulate a 'framework policy', 'liberal interventionism', and 'structural policy' for the market economy to function well, and advocated the 'principle of subsidiarity' for the decentralization of political power.

Finally, in chapter 13 Makoto Tezuka explores the Social Market Economy, a concept that has dominated the political economy of Germany since the end of World War II. The term was coined and developed by Alfred Müller-Armack. Tezuka investigates the influences of the German Historical School on the structure of the concept. He demonstrates that the Social Market Economy is neither a liberal economy nor a mixed economy but a system based on the integration of the economic mechanism and social ethics. It is argued that the notion of society as an organic whole is the core of German historical thought and a belief in life in particular must be an organizing principle of the Social Market Economy.

Chapter 1

Rational reconstruction of the German Historical School

An overview

Yuichi Shionoya

Historicism in economics originated in Germany in the latter half of the nineteenth century. According to the accepted view in the history of economic thought, the German Historical School had three generations: the Older Historical School (Wilhelm Roscher, Karl Knies, Bruno Hildebrand); the Younger Historical School (Gustav von Schmoller, Lujo Brentano, Karl Bücher, Friedrich Knapp, Adolph Wagner); and the Youngest Historical School (Arthur Spiethoff, Werner Sombart, Max Weber) (Schumpeter 1954:807–20). Can one develop a unified picture of the German Historical School from these diversities? If so, in what sense and how?

Introduction

The German Historical School has been described as a criticism of British classical economics. In opposition to the universally valid economic theory, it asserted that economic principles should be inductively derived through the study of historical facts of different countries. However, that was an immediate moment; the root of the Historical School must be found in German romanticist, idealist, and nationalistic ideology which was a reaction to rationalism and enlightenment, of which classical economics was one of the products. Therefore, it is understandable that German thinkers such as Johann Gottfried Herder, Adam Müller, and Friedrich List are sometimes regarded as the forerunners of the Historical School.

Quentin Skinner (1969) discussed two approaches to interpreting texts in the history of ideas: one is to emphasize the total historical context in which any text is located; the other is to derive from the text universal propositions apart from the context of history. The two approaches may be called contextualism and textualism. In the same sense Richard Rorty (1984) distinguished the methods of description in the history of philosophy as historical reconstruction and rational reconstruction: the former places the text in question in the context of the past and identifies what it wanted to say; the latter interprets the text from the standpoint of the present and specifies what it could have said in terms of ideas unknown to the original

authors. The distinction between 'meaning' and 'significance' may also be attributed to the goals of the two methods of reconstruction, respectively.

The German Historical School can be reconstructed in terms of a historical as well as a rational context. According to the German perspective, the organicist *Weltanschauung* was politically oriented toward industrialization of less developed Germany and concerned with the building of an institutional framework on a national basis and thus could not accept British *laissez-faire* economics. But the importance of the German Historical School cannot be overemphasized in its historical role alone. The fact that its thought was partly implanted in other countries—e.g., Great Britain, the United States, and Japan—in its heyday and that some of its influence was revived in Germany after its decline reflects its universalizable elements. Despite divergences among the members of the school, its intellectual project can be generalized through an interpretation and reconstruction of the scope and method of economics; this suggests a new perspective that may provide an alternative to present-day mainstream economics. This chapter presents the framework for a rational reconstruction of the German Historical School, and explores the relevance of its thought to current evolutionary and institutional thinking.

Evolution of the mind and society

Social science observes social reality and constructs theory, which, in turn, becomes an object of observation. Social science is thus characterized by its duality: it addresses social reality and its achievement becomes an object of social science. These dual aspects of social science can be represented by the notion that the mind and society interact in a historical process.

In this sense, suppose that there are two objects of study in social science: society and the mind, or economy and economics, as far as economic science is concerned. The former relates to a whole group of real and organizational factors of society and the latter to spiritual and ideational factors of society. We will assume that the system of theory addresses society and that the system of metatheory addresses the mind. Theory in economics comprises economic statics, economic dynamics, and economic sociology, which differ in scope and method as they relate to an economic society. Metatheory, which considers the mind or thought, is a theory about theory and consists of the philosophy of science, the history of science, and the sociology of science. Thus the structures of theory and metatheory are parallel in the sense that in social science both society and the mind are analyzed at three levels: the static, the dynamic, and the social. The two structures can be interpreted as the system of theories for two different social areas: the mind and society. I call this concept of social science a two-structure approach to the mind and society (Shionoya 1997:262–5).

From this observation it can be inferred that just as a social study, whether historical or theoretical, focuses on social reality and attempts to make a subjective construction of the reality, so a study of theories is merely a subjective construction of those theories because they are part of social reality. Studies conducted in the past, which may be classified as culture, science, thought, or whatever, are now part of the social reality. An approach to previous studies, whether an interpretation or a critique, is also either historical or theoretical.

Figure 1 summarizes the two-structure approach to the mind and society, which I developed through an inquiry into the work of Joseph Schumpeter. Contrary to the conventional view, I believe that Schumpeter should be regarded as one of the successors of the German Historical School because he attempted a rational reconstruction of that school, especially Schmoller's research program, in terms of economic sociology and made his own contribution from this perspective (Schumpeter 1926). The framework of his approach thus will be useful in reconstructing the Historical School.

The left side of Figure 1 shows that substantive theory addresses social reality or the real aspects of society and attempts to subjectively construct the reality, where three levels are distinguished in theoretical or historical investigation. When the focus is on the economy, the levels of economics include economic statics, economic dynamics, and economic sociology. The right side of the figure shows that metatheory is merely a subjective reconstruction of mind products or scientific theories, which consist of the philosophical, historical, and sociological investigation of thought and science. Rorty's distinction between historical and rational reconstruction is the first approximation that does not distinguish between types of metatheory.

The important conception underlying the two-structure approach is that interactions between the mind and society shape historical evolution and that the mind and society are two aspects of the same evolutionary process. In Schumpeter's view (1954:137), this recognition is attributable to Giambattista Vico, the eighteenth-century Italian thinker. Because Vico is regarded as the first serious critic of Cartesian rationalism and the founder of nineteenth-century historicism, I argue that the evolution of the mind and society is key to understanding the German Historical School, which took ethics seriously as a determinant of social schemes in an evolving process.

Attempts to explore the interactions between the mind and society are illustrated, among others, by Karl Marx's distinction between the substructure and superstructure of society, Weber's association between the Protestant ethic and capitalism, and Schumpeter's thesis that capitalism will fall because of its moral failure resulting from its economic success. These attempts are understood in light of the two-structure approach that models the research program of the German Historical School.

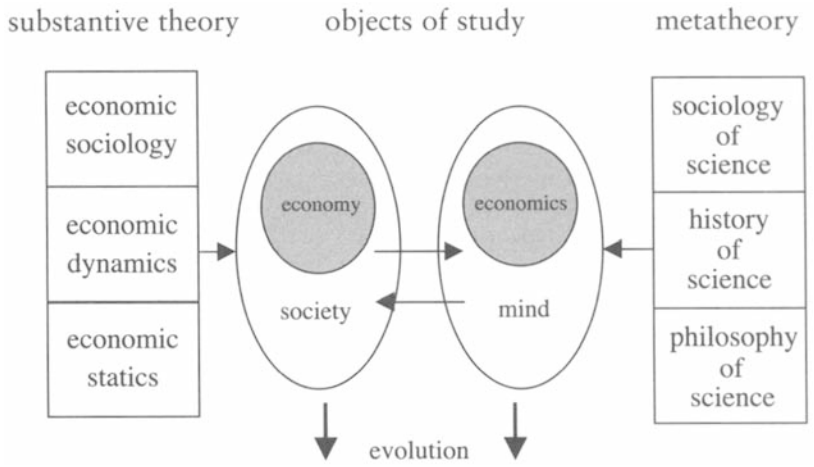

Figure 1 Two-structure approach to the mind and society.

Source: Yuichi Shionoya, *Schumpeter and the Idea of Social Science: A Metatheoretical Study,* Cambridge University Press, 1997, p. 265.

Schumpeter (1914:110–13) summarized six basic perspectives of the German Historical School: (1) the unity of social life, (2) a concern for development, (3) the organic nature of society, (4) the plurality of human motives, (5) individuality rather than generality, and (6) historical relativity rather than universality. Of these perspectives, Schumpeter attached much importance to the combination of (1) and (2), contrary to the standard view of historicism, which emphasized the combination of (2) and (5), as was evident in the work of Ernst Troeltsch and Friedrich Meinecke. In a historical process, according to my interpretation of Schumpeter, all aspects of society change through multifarious interactions; this entails endogenous development or evolution because all social factors are included in the process. Interrelationships between the mind and society represent a simplified model of this process and are the object of economic sociology, in which historical individuality is incorporated into an appropriate theoretical schema such as typology or stage theory. I will now discuss how the German Historical School is restructured as a theoretical scheme that deals with an evolutionary process by means of the historicalethical method.

Historical-ethical method

Schumpeter (1914:100–1; 1954:809–14) argued that the German Historical School was developed as a genuine school under Schmoller's leadership.

This is how Schumpeter interpreted the rational reconstruction of the Historical School. Schmoller (1897:26) called his method 'historicalethical': this sloganistic advocacy of method is merely a rational reconstruction of the school that would serve as a strategy for its integration and development in the future. Elsewhere I have examined Schmoller's research program in greater detail and argued that much of his program should be revised from the viewpoint of rational reconstruction (Shionoya 1995).

On the basis of this dual method, the Historical School opposed not only British classical economics but also contemporary German and Austrian neoclassical economics. The latter confrontation included the *Methodenstreit* between Schmoller and Carl Menger and the *Werturteilstreit* between Schmoller and Max Weber. Although it is commonly believed that Schmoller lost both battles, such an outcome was not necessarily the result of rational investigation. To discover clues to a rational reconstruction of the German Historical School, let us analyze the significance of the historical method and the ethical method in economics separately.

Empiricism versus rationalism

In the *Methodenstreit* the historical method, or empirical and inductive method, was diametrically opposed to the abstract, theoretical, and deductive method, and the relative superiority of the two methods was the bone of contention. But even for Schmoller the historical method was not simply directed to the accumulation of historiography and historical monographs; rather, it aimed to gather materials to ultimately build a broader theory for the institutional framework of the economy and its historical changes.

In hindsight it is pointed out that the real issue in the *Methodenstreit* was not methods as such but problems to be pursued: *utility and price* or *institution and evolution*. Neoclassical economists focused on the former, whereas historical economists addressed the latter. A method's validity and effectiveness depends on the problems: for the Historical School, the method based on *history and ethics* was advocated to deal with the problem of *institution and evolution*. In later years, in recalling the *Methodenstreit,* Schmoller (1911:479) acknowledged the relationship between methods and problems.

Even the controversy was not inevitable. Although Schmoller's historicalethical method mainly focused on explaining the institutional foundations of the economy, he admitted the value of the neoclassical analysis of utility and price within the framework of institutional analysis. His comprehensive, two-volume *Grundriss der allgemeinen Volkswirtschaftslehre* (1900–04) was an attempt to develop a system of economics on the basis of historical knowledge; in other words, he intended

to integrate two economics. Whether he succeeded or not is another story. The study begins with the 'anatomy' of the institutional framework involving ethics, then argues the 'physiology' of economic circulation in terms of price and income, and concludes with his observations on the development of society as a whole.

Schmoller (1888:147) held that the development of human recognition takes place as the alternation of rationalism and empiricism; instead of making a rash generalization on a poor empirical basis, one should engage in empirical research before launching into the theoretical treatment of historical materials, insofar as the major object of economics is the evolution of economic institutions in a historical process.

The lesson of the *Methodenstreit* is the recognition that new theories would be formulated through feedback between theoretical and historical approaches. To permit continuous feedback, we should make explicit the research task for which cooperation between theory and history will be most necessary and feasible. The need for as well as the difficulty of such cooperation will increase as one goes up the layers from economic statics to economic dynamics to economic sociology (see Figure 1). Schumpeter (1926) defined Schmoller's historical method as the prototype of economic sociology, the theoretical discipline for the development of institutions in terms of interactions among individuals. Schumpeter (1954:20) later coined economic sociology as the generalization, typification, and stylization of history by means of institutional analysis and located it as one of the four disciplines in economics beside theory, history, and statistics.

The fundamental defect of the historical method in the German Historical School was the methodological view that theory or law must be a summary or generalization of empirical facts. Since it is extremely difficult to acquire information about the total historical development of economic life, a theoretical formulation based on the historical method would never be attained within a finite time. The school's opposition to simple and unrealistic assumptions in theoretical economics was also derived from this naïve empiricism. When Schmoller (1911:467–8) considered the nature of concept formulation, he argued that concepts are an auxiliary means to organized thought, not a perfect copy of reality, admitting nominalism instead of realism. But because he believed that the ultimate goal of science was still realism, he suffered from the serious contradiction between nominalism and realism.

To utilize feedback between theory and history, one should not wait until extensive data are collected in order to endow concepts with as rich an empirical content as possible. From nominalism it is only a step to instrumentalism, the view that theories are not descriptions but instruments for deriving useful results and are neither true nor false. Instrumentalism asserts that assumptions or hypotheses are arbitrary creations of the human mind and need not be justified by facts, and that theories deduced from

assumptions are not descriptive statements in themselves but instruments for understanding and explaining facts. Although a collection of historical facts is welcome, economic sociology based on the historical method should be formulated on the methodology of instrumentalism.

Schumpeter, adapting instrumentalist methodology to economic sociology, carried out a wide range of investigations mainly in terms of the interactions between economic and non-economic phenomena, treating non-economic elements as a set of social institutions surrounding the economic area (Shionoya 1997:193–222). It should be noted that Max Weber also tried to develop a solid foundation for economic sociology by linking economic phenomena with political, legal, and religious phenomena (Swedberg 1998). His methodology of ideal type was a version of instrumentalism specifically applied to the historical method (Shionoya 1996). In addition to the work of Schumpeter and Weber, it is possible to add Werner Sombart's threefold approach of economic spirit, order, and technology to see what the rational reconstruction of the German Historical School has produced: all three scholars contributed to the development of an economic sociology that was based on the substantiation of the historical method as it applied to the interactions between economic and non-economic areas.

Morality versus self-interest

The second distinctive feature of the German Historical School is its emphasis on the ethical method. Although it seems generally accepted that Schmoller was also defeated in the *Werturteilstreit,* that is not a valid interpretation. It is indeed true that ethical value judgment was denied by Weber's thesis of value freedom in science. But this means neither that social science should not deal with value judgment, nor that Schmoller's ethical method should be rejected simply because of its value-ladenness.

To avoid misunderstandings about the German Historical School and to attempt its rational reconstruction, it should be noted that the ethical method as a scientific method implies a hypothetical assumption in economic theorizing. It assumes that human behavior is motivated by various considerations other than self-interest, including morality, law, and customs. If this were the expression of value judgment, the assumption of the self-interested man in mainstream economics, which was ridiculed by Thorstein Veblen (1898) as a 'lightning calculator of pleasures and pains' and by Amartya Sen (1977) as a 'rational fool', would have been condemned as a sort of value judgment commending egoism. In fact, Schmoller did not advocate any subjective value judgments, but dealt with the evolution of the historical process in which ethical values are developed as a matter of facts and tried to explain the reality in terms of broader human motives. In his view, values in the form of law, morality, and customs are embedded

in institutions and play a leading role as the determinants of evolving institutions and of consequent economic performance.

Schmoller (1911:437) asserted that the ethical approach not only aims at the recognition of moral facts that are embedded in social institutions but also is conceived in a teleological form. The nature of teleology in Schmoller is quite important in appraising his ethical method but has been little noticed. From the Kantian teleological perspective, society is assumed to have certain ends that are explained as if human actions and social systems might work spontaneously and reciprocally to achieve those ends based on the teleological relationship between ends and means. If a society can be regarded as a unified entity with its own ends—in other words, if holism can be assumed—a teleological inquiry is useful to make an estimate of the world about us in terms of the relationship between ends and means. Since moral values are to govern society as a whole, teleology is effective in the study of institutional organizations embodying ethics.

The principle of teleology cannot be used for cognitive purposes in the strict sense; it can be employed only by reflective judgment to guide an investigation of an organic entity. Schmoller regarded teleology as a heuristic device that supplements an empirical study when historical knowledge is insufficient. Teleology assumes that individuals behave as if they would purposefully serve the ends of the whole. For Schmoller, the leverage for this purpose was ethics of justice. The teleological ends would be realized in an evolutionary process based on interactions between ethics and institutions. Schmoller's teleology relates to methodological holism and has nothing to do with the justification of a specific ideology.

The ethical method thus has two functions in historical economics: first, ethics is understood empirically as a determinant of human behavior and social systems; second, it is assumed methodologically as a teleological principle of social inquiry. In restructuring the German Historical School, the combination of methodological holism and instrumentalist methodology will provide the historical-ethical approach with a legitimate foundation. In other words, the status of ethics in the Historical School should be interpreted as a value premise, not as a value judgment.

Institution and evolution

The German Historical School is characterized by the unique attempts of the stage theory of economic development. Schmoller (1900–4, 1:53–7) in particular tried to formulate a stage theory of institutions in terms of the interactions between economy and ethics. He distinguished social systems in the family, the regional community (village, city, and state), and the commercial firm. Each system is based on a different organizational principle: sympathy, kinship, and love for the family; neighborhood, nationalism, law, and coercion for the regional community; contract for the

firm. What Schmoller meant by the ethical determinants of institutions relates to these principles. Contrary to a self-interest model of economy, historical economics pays attention to a community in which individuals share common values and the public interest in pursuing economic activities on the basis of their culture, history, and traditions.

From autarkic family economy or tribal economy there developed two types of organization. On the one hand, organizations of the regional community such as village economy, city economy, territorial economy, and national economy were formed for the purpose of controlling economic life and serving the public interest at different levels of the regional economy. On the other hand, commercial firms were developed as organizations to pursue profits, and the private enterprise system entailed various institutional arrangements such as the division of labor, markets, social classes, property ownership, and so on.

Schmoller's scheme of development in stages from village economy to city economy to territorial economy to national economy was based on the idea that the institutions of community are the carriers of social policy to control the free play of firms in the marketplace. His stage theory was concerned with the evolution of institutions brought about by the interactions between ethics and economy, between spiritual-social and natural-technical factors. It basically differed from the notions of the Older Historical School that relate to the natural-technical aspects of the economy.

Economics of latecomers

The idea of institutional evolution stressed by the German Historical School has relevance to contemporary thinking in economics and ethics. Several factors are involved in the idea of institutional evolution: first, Germany was a latecomer to the process of industrialization inaugurated by Great Britain; second, the industrialization process is quite diverse across countries; third, a latecomer depends on institutional factors rather than on *laissez-faire* to catch up advanced countries; fourth, institutional development is explained not so much by the free choice of autonomous individuals in markets as by the sense of community and coordinated actions based on shared values.

These themes are integrated in Alexander Gerschenkron's thesis (1962) of economic backwardness, which denies the uniformity of economic development among countries and recognizes a differentiated pattern of development that is systematically accounted for by relative degrees of backwardness. Gerschenkron's thesis represents neither a universal proposition nor a descriptive, unique history of economic development but rather an intermediate schema, i. e. a typology. If all economic phenomena were characterized by perfect uniformity, there would be no reason to talk about institutions for which certain economic phenomena were typified; only

one meaningful institution would exist. On the other hand, if all economic phenomena were *sui generis,* one could not categorize them according to a particular type or group; there would be such an infinite variety of behavioral patterns that it would be useless to consider types.

The concept of institution is essential to historical research in two senses: first, in the cognitive sense, institution makes a typological observation possible despite the seemingly infinite complexity of history; second, in the practical sense, institution is a strategic device of latecomers for catching up to advanced countries through a differentiated growth path based on the degree of economic backwardness. Thus the institutional approach of the German Historical School is not a uniquely historical product but is generalized in the economics of latecomers. Furthermore, to meet the demands of the German Historical School their stage theories should be replaced with typological theories that admit a differentiated growth path instead of maintaining a standard stage sequence.

Communitarian ethics

What constitutes the strategy of latecomers in terms of institutional devices is communitarian ethics. The current debate in ethics and political philosophy between liberalism and communitarianism is, I argue, a reproduction of British classical economics and German historical economics. Community is characterized by common social practices, cultural traditions, and shared values; it is something more than a society of free and autonomous individuals. Communitarians emphasize the social embeddedness of individuals in contrast with liberalism, which stresses individual rights and conceives of the individual as the ultimate source of values.

The controversy between liberalism and communitarianism is not a genuine conflict of values as there was no genuine conflict of methods in the *Methodenstreit,* in which different models of man were disputed between theorists and historians. The two doctrines deal with morality of a different scope: liberalism is concerned primarily with a universal principle of justice to be observed by free and equal citizens, whereas communitarianism assumes the existence of a limited community and is concerned with the common good to be shared with the members of the community. Communitarianism is a version of virtue ethics that should prevail in a community as an institution. Since virtue ethics represents normative values such as excellence, it might fit into the framework of teleological arguments for the evolution of institutions.

Conclusion

In conclusion, the rational reconstruction of the German Historical School suggests that a lot of tasks must be performed to provide an alternative

paradigm to the mainstream with regard to the method, scope, and underlying value premises of social science. Our attempt at the rational reconstruction intends only to offer an overview of the German Historical School from the methodological perspective. Substantive contents should be worked out in various ways at the frontiers of economic research. The relevance of the German Historical School to contemporary ideas demonstrates its challenging potentiality. Let me summarize the skeleton of our observations.

First, the style of economics as was advocated by Gustav von Schmoller for the German Historical School is conceived as an attempt to address the evolution of the mind and society. In the history of economics, this overall approach is comparable only to the work of Marx, Weber, and Schumpeter. Second, to deal with this problem, which naturally went beyond the scope of mainstream economics, the German Historical School proposed the innovative historical-ethical method and emphasized empiricism against rationalism and morality against self-interest. This does not mean the denial of theory but the demand for a new theory.

Third, based on this method, the German Historical School endeavored to develop the economics of institution and evolution, which provided the 'anatomy' of the institutional framework and its evolution in contrast to the 'physiology' of a static economy. The economics of evolutionary institutions entailed the political and moral implications for the catching-up strategy of latecomers and the role of communitarian ethics.

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Chapter 2

Adam Müller's 'Agronomische Briefe'

Tetsushi Harada

This chapter addresses 'Agronomische Briefe' [Agronomic Letters], by Adam Heinrich Müller (1779–1829), which was published in the 1812 volume of the magazine *Deutsches Museum,* edited by Friedrich Schlegel.

Wilhelm Roscher (1817–94), in his 1874 book *Geschichte der National-Oekonomik in Deutschland* refers to 'the economics grouped around Adam Müller' —including the work of Friedrich Gentz (1764–1832) and Karl Ludwig von Haller (1768–1854) —as the 'Romantic School of economies'. According to Roscher, the relationship of this circle to Adam Smith and his school corresponds to the relationship of the Romantics of the Schlegel brothers, etc., to the Classical School in literature. Müller and others expressed a reaction against the rationalizing, centralizing trend of the Enlightenment in the eighteenth century. Maintaining a distance from 'individualistic cosmopolitanism', they stressed 'nationalities situated intermediately between individual men and the whole of mankind' (Roscher 1874:751). Müller's reaction against Adam Smith is 'no blind, hostile one, but an important, and in many ways truly complementary reaction' (p. 763). If Müller had continued to develop in a normal way afterwards, i.e. after the publication of *Die Elemente der Staatskunst* [The Elements of Statecraft] in 1809, he would have 'indisputably become one of the foremost economists of all time' (p. 777). However, since he explained each phenomenon as a competing relationship of two principles according to his own logic of 'contrast' [Gegensatz], he was apt to neglect historical facts that did not accord well with this schematization, and considered the existence of two aspects as a mere parallelism, e.g. as the 'difference between two legislators or even nations', so that he came to overlook the difference between 'two stages of development' (p. 772). Therefore his method of economics is only 'half-historical' (p. 771).

Roscher (1861:14) wrote: 'Only one who knows the general laws of development is able to judge their particular national exceptions and modifications'. For this reason, he intended to extend 'the existing theory' —including the 'general laws of development' —of the Classical School of

Smith and others 'to all nations and times' (Bücher 1894:107), through the recognition of individualities among nations.[1] Therefore, although Roscher expresses his approval of Müller's attitude toward the renewal of economic science through the historical recognition of national individualities, he does not admit a schematization of the kind proposed by Müller against the Smithian general laws of development. But how, exactly, did Müller in 'Agronomische Briefe' conceive of economic development?

In 1842, thirty years after the appearance of 'Agronomische Briefe', Friedrich List (1789–1846) published the article 'Die Ackerverfassung, die Zwergwirtschaft und die Auswanderung' [The Land Institution, the Minuscule Farm and Emigration], one of the most important works on agronomy in the first half of the nineteenth century. In his book *Das nationale System der politischen Ökonomie,* which came out the previous year, List advocated trade protectionism as a means of allowing latecomer capitalistic countries such as Germany to catch up with the leading industrialized country, England. In this connection, he expresses himself on agriculture in the 1842 work in the following way.

Along with the fostering of national industries, 'what the industrial population needs in the way of raw materials and provisions must necessarily be supplied as a surplus from the agricultural population, and only by means of this surplus is the agricultural population placed in a position to purchase the products of industry and of foreign regions in abundance' (List 1842:444). With such remarks, List intended to build up a modern commercial agriculture able and prepared to exchange its products commercially for domestic industrial products and foreign commodities. As far as domestic relations are concerned, this represents List's ideal of a balanced national economy in which 'agriculture, industry and commerce' are to be developed 'in a proper relation' (p. 444). The core of the national economy, in his view, is that the broad domestic market consists of both an industry made robust through protection and an agriculture sufficiently large to counterbalance it, and that exchanges take place in the domestic market between these two balanced branches. According to this view, either of the two extreme types of agricultural holdings, namely, 'large farms' [Großwirtschaften] or 'minuscule farms' [Zwergwirtschaften], induces poverty and proletarianization among the lower strata of the agrarian population, which are serious obstacles to building a sound nation-state. Therefore, independent 'medium and small farms' [mittlere und kleinere Wirtschaften] are desirable. Many farms on this scale should be created, first, through the 'rounding of estates' [Gutsarrondierung] (pp. 435–6, 451). However, it is impossible by this means alone to increase the scale of domestic agriculture enough to provide a balance for a developing industry. List further proposes that, to solve this problem, medium and small German farms should be extended geographically through colonization, especially 'emigration' (p. 491) into the Hungarian region. In this respect, in fact, we

could say that List indirectly advocated a quasiimperialistic expansion of Germany against France and especially Russia.[2]

List's intentions were to modernize and industrialize Germany as a nation-state so that it could compete with the most industrialized country, England, to build up a commercial agriculture of medium and small farms as a counterbalance to domestic industry, and to promote land consolidation and colonization, while at the same time opposing—even by military force—the surrounding nations that confronted Germany 'right and left' and hindered its colonization projects. But from another point of view, List can also be characterized as a kind of romanticist, for with his images of medium and small farmers, i.e. a 'middle class' (pp. 471–2), he was in effect adopting Justus Möser's (1720–94) concept that was modeled on the independent farmer of ancient Germany.[3] There is no lack of foundation, therefore, to Noboru Kobayashi's argument that List's views could, through the agriculturalists at the end of the nineteenth century, be carried over into the German expansionism of the first half of the twentieth century, when we find the two characteristics, expansionism and romanticism, combined in List.[4]

As far as the eighteenth and nineteenth centuries are concerned, this point should be examined in Möser's own writings, particularly with respect to whether his thinking contained invasionist elements, but this would go beyond the scope of this chapter, whose main concern is Adam Müller. The following account explains the agronomic thought of Müller as the prime representative of the Romantic School and then compares it with the agronomic and expansionistic thought of the modernist List.

Mercantile agriculture and isolated agriculture

In 'Agronomische Briefe' Adam Müller distinguishes two ideal types of agriculture based on whether or not it is carried on mainly for commercial purposes, especially foreign trade.

The first type is 'isolated agriculture' [isolirte Landwirthschaft], i.e. 'national'- or 'old'-type agriculture. Farms of this kind 'are almost completely based on their own resources, live off themselves and are thus independent of world trade and its fortunes'. The second type is 'mercantile agriculture' [merkantilische Landwirthschaft], i.e. 'rational'- or 'so-called new'-type agriculture. Farms of this kind 'remain dependent on a particular market and on the sale of their products, and therefore on the grand occurrences in the world'. In this distinction, though Müller does not make an explicit issue of the difference of farm scales, 'isolated agriculture' has less 'dependence on money' and more 'personal and *generous* service relationships', and 'mercantile agriculture' has more 'dependence on money' and on 'the works of the *day-laborer*' [Arbeiten des *Tagelöhners*] (Müller 1812:135–9; Müller's italics).

According to Müller, 'mercantile agriculture' was dominant in England, whereas, if anything, 'isolated agriculture' was predominant in continental Europe. Yet even in Europe, especially Germany, 'mercantile agriculture' was quickly and rashly spreading as a result of its promotion by Albrecht Thaer (1752–1828) and others; thus 'isolated agriculture' was in the process of being considerably encroached on.[5] Müller found this to be a grave state of affairs and advocated maintaining 'isolated agriculture' in Germany. His argument rested on three points: first, the need to learn a lesson from the blockade of the Continent and its consequences; second, differences in economic and institutional conditions in England and Germany; and third, the problematic nature of 'mercantile agriculture' itself.

The lesson from the continental blockade

Regarding the first point, Müller makes the following observations about Napoleon's blockade of the Continent during 1806–14.

In 'certain coastal regions' of Germany, 'mercantile agriculture' had formerly been introduced in a number of 'happy experiments' (p. 142), because the districts were geographically suitable for it. Afterwards, however, circumstances were considerably changed owing to the continental blockade. The farmers' relations with foreign markets—on which they had depended for trade in grain, wood, and cotton—were now broken off. Therefore, even in their innovative use of 'old' soil, they had to 'strive to subsist in themselves'. 'Mercantile speculations in landed property and its products must diminish, and the true unadulterated character of national agriculture must emerge again from the whirlpool of experiments and circulations of goods' (p. 149).

Having seen the way in which Napoleon's blockade had made trade with England out of the question and 'mercantile agriculture' in the coastal regions therefore impossible to carry on, Müller perceived that the risks of an agriculture that depended on foreign trade and was easily influenced by 'grand occurrences in the world' were too great. Because 'mercantile agriculture' quickly became impossible to pursue in the event of blockades, wars, and so on, if allowed to occupy too dominant a position in German agriculture as a whole, one or another of the 'grand occurrences in the world' could destroy agriculture altogether, or even the entire national economy. With warnings of this kind, Müller opposes the excessive spread of unstable 'mercantile agriculture' and advocates a healthy return to 'isolated agriculture' in Germany's coastal regions.

Economic and institutional conditions in England

Second, Müller notes the conditions in England that were different from those in Germany.

One economic characteristic of England was 'the enormous capital of this nation', which was sufficient to set agricultural production 'into mobilization', i.e. to commercialize it. In this respect the country was well suited to 'merchant agriculture'. Furthermore, although 'mercantile agriculture' was now predominant in England, the problem of 'grand occurrences in the world' had not become acute there. Even when such an event did arise, it hardly had the effect of throwing the national economy into confusion, because England already possessed both a 'world market, which allowed English farmers to make large-scale experiments', as well as varied and extensive 'land and water communications' (p. 141) not seen in other nations.

Concerning the negative domestic effects of 'mercantile agriculture', it was regarded as normal that people of the lower classes should be employed as 'day-laborers' on farms and might be allowed to sink further into helplessness because of commercial fluctuations. At the same time, however, a relief system for them based on England's 'poor law tax' (pp. 141–2) enabled the government to cope with the problem. Moreover, because that country had managed to preserve its 'inviolate sacred laws of the state', above all its 'inviolate legislation' [unverletzte Gesetzgebung] — institutions that in Germany had been destroyed during the Thirty Years' War[6]—'all national needs', including non-commercial ones, were taken into account during 'parliamentary debate', so as to restrict or at least mitigate the effects of the dominance of commercial interests. In this respect, Müller considers that 'the theory of Adam Smith' —according to which almost everything is entrusted to the market and to commerce—has in fact only 'a relatively slight influence' 'on the legislation of his native land' (pp. 142, 146).

For Müller, the heart of the problem was that the 'German eulogists of English agriculture' (p. 142) advocated the expansion of mercantile agriculture despite these differences between England and Germany. In Germany, which lacked the required economic and institutional conditions, the spread of mercantile agriculture was difficult, and if mercantile agriculture were to become predominant, a very dangerous situation could arise because of the country's insufficient ability to cope with its negative effects.

The problem of mercantile agriculture per se

Then, are we to assume that Müller was proposing that Germany's agriculture and national economy be developed through the creation of the same conditions that existed in England? In grappling with this question, we must scrutinize more closely the third argument he raises against the excessive spread of mercantile agriculture, namely, the problems of mercantile agriculture itself and the significance of the role played by isolated agriculture in the national economy.

For mercantile agriculture, the principal aim is to make money, and both its markets, where mercantile farmers earn their living, and especially its trading partners—who supply the goods of exchange—are normally located far away from the region where the agriculture is carried on. Mercantile agriculture is thus directed to satisfying the needs of distant or foreign, unknown people. Therefore, not only does this kind of agriculture bring instability owing to its dependence on foreign markets, but also it fails to satisfy the 'wants of the immediate surroundings'. Mercantile agriculture is 'the extension of a city economy' (p. 158). As part of a city economy it may indeed have a certain significance, but as an agriculture it cannot contribute to the development of a balanced system of economic relations in each local region. 'God's wish is for a natural [land system], i.e. such a one as is grounded on the wants of your nearest surroundings, or your immediate neighborhood which you can survey' (p. 145). The task of constructing this system cannot be entrusted to mercantile, but only to isolated agriculture.

Müller conceives of ideal agriculture as an 'eternal marriage of a people with a certain soil', and asserts that 'all prosperity and all growth, all inward organic cultivation, all proper vigor' depend on this 'marriage'. This means that a 'people' settles on a certain 'soil' and builds up a 'stable state' of the balance of production and consumption in each region, and that historically, on this basis, spiritual and institutional relationships develop in such forms as family ties linked with the possession of land, as a set of 'hereditary service relationships' in a region, and as bonds of 'personal services' between individuals and the state. According to Müller, the whole system of these 'organic' relationships—which exceeds the mere 'sum of individual powers'—ensures the stability of the nation-state and is supported by isolated agriculture. In this sense, this type of agriculture is the 'stem and root of all political life'. In contrast, mercantile agriculture— which should be stamped as having a 'nomads character' (pp. 147–8) —is incapable of constructing stable relationships in a district; rather, it is always in search of contacts with far-off regions and, in the process, makes the state unstable.

The 'hereditary service relationships' that go together with isolated agriculture originate in feudalism, so that Müller's commitment to a protection of feudalism is obvious. The service relationships of peasants to their lord are characterized by 'love, free obeisance and community' (p. 183); services are seen not as compelled, but as offered of the peasants' own accord in return for the lord's benevolence in their community. Most important is the point that in isolated agriculture there is 'a noble personal reciprocity of obligations' [eine edle persönliche Wechselverpflichtung] between lord and peasants based on their mutual reliance. As the 'care' [Sorge] (Müller 1819a:232) of peasants by the lord is later mentioned by Müller in his 1819 book *Von der Nothwendigkeit einer theologischen*

Grundlage [On the Necessity of a Theological Basis], it appears that the lord, in return for his peasants' service to him, has a *de facto* obligation to relieve those who suffer extreme poverty, e.g. because of a disaster. But where isolated agriculture is dissolved, 'a Roman obligation, i.e. slavery' emerges between lord and peasants; in other words, the lord's obligation to relieve his peasants disappears, and 'immense and indissoluble systems of debt' [Schuldensysteme] (Müller 1812:183–4) arise, in which nothing remains but the obligation of peasants to give their lord money.

Precisely what kind of relationship does Müller envisage with this concept of 'systems of debt'?

He writes: in mercantile agriculture, 'only one substitute, i.e. money payment, was given for the old fief and service relation. The new liberty, the earnestly desired freedom of disposability was only realized by means of money. The abolishment of feudalism remained an empty gesture without the establishment of a corresponding money power' (p. 185). Here Müller is referring to the realities of 'the new liberty, the earnestly desired freedom of disposability'—namely, that with the abolishment of feudalism estates could be freely disposed of and peasants could hold land, but in the process there was the simultaneous 'establishment of a corresponding money power'.

It should be noted that Müller's account makes no mention of regional limitations in more industrialized countries such as England. We therefore need to consider the situation in the German states of that period, above all Prussia. The liberation of peasants from their previous condition of bondage based on the relationship of estate feudality, i.e. Gutsherrschaft, was decreed in Prussia as early as 1807 with the October Edict. But the *de facto* abolition of Gutsherrschaft and the accession of peasants to land ownership came about several years later, through a series of legislative measures to increase tax revenues, beginning in 1811 with the Regulation Edict [Regulirungsedikt] and continuing over the next ten years or so.

The Regulation Edict played a decisive role in the dissolution of agricultural feudalism in the sense that it clearly spelled out the abolition of peasants' obligatory service and contributions to their lord, and recognized their right to acquire lands as their own properties. It was ruled that (1) peasants should in principle obtain the property rights to the lands they currently cultivated, but that (2) one-third of these lands (in the case of peasants cultivating hereditarily) or one-half (in the case of peasants cultivating non-hereditarily) must be returned to their former lords as 'reparation' for their yielding of the property rights, and (3) the lords should henceforth be exempted from their traditional duty to care for their peasants. These terms were hard on the peasants, or ex-peasants, for even if they returned only one-fourth of their cultivated land, it might still be difficult for them to manage the remaining three-fourths, and they might well have been 'in danger of becoming day-laborers' (Knapp 1927, 1:166, 170). When their living conditions deteriorated, they could no longer expect any relief

from their ex-lords. And if they chose to return a smaller than stipulated part of their lands to stave off ruin, they had to pay the lords a corresponding amount of money. But in such cases, since peasants normally had no money of their own, they had no choice but to repay their enormous debts little by little.[7] We may assume that Müller's concept of 'systems of debt' in the 'Agronomische Briefe'—which were published the year after the Regulation Edict—reflects his own grasp of this situation.

In February 1811 a petition composed by Müller under the signature of a career officer, Friedrich August Ludwig von der Marwitz (1777–1837), and lodged with the state chancellor Karl August von Hardenberg, advocated the confirmation of traditional status systems and the retention of old forms of land-ownership.[8] Marwitz, an ally of Müller's in the campaign against the reforms, asserted that it was erroneous to consider the traditional institution as 'bondage' [Leibeigenschaft]: 'this condition, on the contrary, has just begun. It is the bondage of the smallholder to the creditor'. Once the lords' obligation to care was abolished, ex-peasants not only suffered the weight of massive debt, but also were forced to look for work as 'agricultural laborers'. When they found no work, they were 'dependent on begging or left to starve' (Lütge 1933:495).

Marwitz and his fellow campaigner Müller were indeed defenders of feudalism, but not of the kind who stood by certain lords and other aristocrats in their attempt to transform themselves into entrepreneurs of mercantile agriculture. These aristocrats effected this transformation by taking advantage of the reforms and the abolition of their traditional obligations to care for peasants.[9] Marwitz and Müller had a genuine concern for the livelihood of peasants who lost the support of their lords and then sank into poverty through the shrinking of their cultivated lands after the abolishment of feudalism. The two activists did what they could to maintain the traditional 'noble personal reciprocity of obligations' between lord and peasant, observed as a spiritual bond in accordance with what they saw as the essence—ideal—of feudalism:

> The present state of affairs is that the public and military services, the teaching profession and almost all the higher and personal offices of civil life have taken on the characteristics of business and wage labor. Only the service relations of agriculture now remain, but do you wish to concent to the total abolition of these? Which people are willing to pull up this last root, when through it all the small trivial businesses, all the transient possessions are connected with the fatherland's soil and its permanence?.... If we make our agriculture mercantile, our national existence and the entire and sole security for our particular existences are lost, all the proper values disappear and only the prices of things are left.... [This situation appears] when we forget [the preeminence of] the personal over the material, being

> over having, the spirit of freedom over the brutish impulse of urgent need.
>
> (Müller 1812:171)

With words like these, Müller deplores the loss of the 'noble personal reciprocity of obligations' and pleads for the preservation of the 'last root' of this relationship in the area of agriculture, especially isolated agriculture. He casts fundamental doubt on the notion that each individual or each group in a national economy simply aspires to acquiring values from 'having' quantitatively larger amounts of money, rather than from the meaning of individual lives, including their spirituality. He deplores the way that individual lives have become unstable owing to their dependence on the fluctuating 'prices of things'.[10] Thus, from his historical position at the beginning of the commercialization of German agriculture, he opposes the 'Reforms' and their tendency to transform all cultivation into mercantile agriculture. This argument includes, even at this early stage, the kind of criticism of overdominant material and monetary relationships that still is valid in our own contemporary society.

True advances

Hardenberg had no liking for Müller, who disturbed the processes of the 'Reforms', and banished him from Prussia at the end of May 1811, under the pretext—as explained to Müller—of sending him as a confidential agent to Vienna to observe the situation there. At the beginning of his stay Müller, as a dubious character from Prussia, was watched by the Viennese police. But he gradually took root in the Austrian capital with the help of social acquaintances, including not only his lifelong friend and adviser Friedrich Gentz but also the brothers August Wilhelm and Friedrich Schlegel, Franz von Baader, and others. It was in these circumstances that he published the 'Agronomische Briefe' in *Deutsches Museum*.[11] In 'Agronomische Briefe' Müller makes the following observations about Austria:

> No other European state has remained so exempted from the rage for business in agriculture but Austria…. Feudalistic agriculture stands unconquered in Austria… The endeavor of an enlightened government to arouse manufacturing industry, to vitalize trade, to promote circulation—such an endeavor as this can in fact operate only beneficially and refreshingly here, because a mighty counterweight exists, fully independent of the systems of this era…. Now, when I look at other European states which—in your opinion—should be commercialized once and for all and regardless of anything, then I am sorry to say that no exception to the eternal principle of the combination of feudalism and mercantilism can be allowed.
>
> (pp. 172–3)

Müller's model of the national economy as an idealization of the medieval state appeared in his 1809 book *Die Elemente der Staatskunst,* in which the balance between feudal agriculture in the country and commerce and manufacturing in the city is the core of the model.[12] This basic concept is still clearly in evidence in 'Agronomische Briefe', where Müller talks about 'the eternal principle of the combination of feudalism and mercantilism'. The reason for his praise of Austria is that 'feudalistic agriculture', i.e. isolated agriculture, still stands as a 'mighty counterweight' to commerce. As long as this 'mighty counterweight' remains, the existence of the nation and the stability of the whole state are assured. In Müller's view, the development of industry, trade and circulation is acceptable in principle and even desirable, provided it is balanced by the stabilizing counterweight of continuity.

In 'Agronomische Briefe', however, the logic of balance between feudal agriculture and urban commerce is more developed than 1809, when it concerned the state of equilibrium in the national economy as a whole. Now the conflict and balance of the two principles are shown as internal relations within the sphere of agriculture. Although Müller regards the attempt to commercialize the whole agriculture of a country as absurd, he does admit that, provided feudal agriculture remains stably rooted, the prosperity of mercantile agriculture alongside it is also desirable. In his own words, 'because I wish for genuine advances in agriculture, and even— to a certain degree—for the spirit of speculation in the area of the agricultural economy, I defend the main condition for all true advances and all continuing mercantilism, that is, the [continuance of the] old agronomic system' (pp. 176–7). 'All true advances' [alle wahre Fortschritte], namely, those producing beneficial evolution in all branches of the national economy, involve growth or development under the condition of existing isolated, feudal agriculture, which operates as the effective counterweight to mercantile agriculture. The sound development of the national economy as a whole can be realized through the functioning of isolated agriculture, which corrects for instability in the national economy induced by urban commerce and mercantile agriculture and for the negative effects of materialism and mammonism.

Whereas *Die Elemente der Staatskunst* considered the whole of agriculture in its feudal aspect as the balancing counterweight to urban commerce and industry, 'Agronomische Briefe' presents isolated, feudal agriculture as one of the two forms of agriculture—isolated and mercantile. In this sense Müller can be said to be more receptive to mercantile elements than before. He appears to be striving to take into account 'what all of our state philosophers wish for', but 'only in some solid way and in a form that it can remain and continue' (p. 178).

The significance of mercantile agriculture, relative as it is, he explains as follows. 'If all those engaged in agriculture should wish to pursue the same path [of isolated agriculture], the funds would be absolutely lacking,

and the profits would drop down to a common level, which would not rise at all above the previous level of national wealth, although it is true that we would not then need to face general disruption and indebtedness' (p. 176). In this sense, Müller too considers mercantile agriculture as necessary for the increase of national wealth. However, the problem is one of degree. In Müller's view, a nation should 'grant not privilege indeed, but precedence' to isolated agriculture, which has 'grown up in a region over the centuries', rather than to the 'rational' model of mercantile agriculture (p. 151). Comprehensively interpreted, Müller advocates either a complete balance of isolated and mercantile agriculture or a situation in which isolated agriculture is somewhat preeminent over mercantile agriculture. In any event, he is adamant that mercantile agriculture should not dominate the isolated kind. This is the primary condition for the ideal development of a national economy, i.e. for the 'true advances' of its organically related branches.

Müller's ideal of 'true advances' centers on the concept of growth in a national economy as conceived from the following viewpoint. The increase of material wealth is certainly desirable, but if its attainment means that as a consequence the entire national economy will become unstable, that the nation will lack any reserve of security against times of emergency, and that materialism or mammonism will arise at the expense of cooperative relationships, then it may be wise to restrict commercial activities. Above all else, the indigenously developed isolated agriculture that has grown up in a region over the centuries constitutes the basis for all other branches of the national economy; thus the foremost task of statesmen is to maintain and, indeed, to strengthen isolated agriculture. With isolated agriculture, the appropriate relationships of supply and demand that have evolved in each region together with cooperative 'service relationships' will thrive not only at the regional level, but also at the state level. This will ensure the stability of the entire national economy, so that even commerce and mercantile agriculture can develop steadily.

Concluding remarks

Müller found it more important to protect—or at least not to weaken—the existing spiritual and material life of the nation through the maintenance of cooperative relationships in domestic production, than to acquire great material wealth through the stimulation of trade and industry for world markets. Although his view of 'true advances' could accommodate a gradual development of trade and industry that does not encroach on the spontaneous and traditional relationships but exists alongside them, he did not, like List, harbor any intention of encouraging the development of a national commercial and industrial power to rival England's. Müller had

doubts about the very idea of material and monetary dominance accompanying a rapid development of trade and industry, and, accordingly, he did not consider the development of modern trade and industry to be a sound basis for a national economy.

List was equally apprehensive about the proletarianization of expeasants and farmers, and wished to prevent it from spreading, but his proposed solutions were the 'rounding of estates' and, where this proved insufficient, a sort of invasive measure, namely the expansion of German 'medium and small farms' into the Hungarian region. To build up a national agriculture that could counterbalance the powerful promotion of industry, as well as to maintain the suitable acreage of farms, List could find no other solution but expansion—expansion of the national territory itself.

Therefore, Müller, who advocated the maintenance of traditional relationships of production—and was in this sense a pronounced Romantic—, was at a far remove from the expansionism of List, who supported the promotion of capitalistic trade and industry and of a corresponding agriculture.

One reason for their difference in outlook can be found in the differing circumstances of the times in which they lived. Müller, in the period of Prussian Reforms, confronted the problem of distressed peasants who were just then being liberated or ejected from the feudal system—including the traditional securities it provided—and assimilated into a system of capitalistic money relationships, with all the confusions this entailed. He did his best to come to terms with these developments, together with Marwitz and others who wished to maintain or revive the old feudal relationships, which they idealized. In Müller's time these were already declining, but survived to the extent that the preservation of the past remained a current issue. On the other hand, by the time of List, capitalistic features were more or less established in German agriculture, so the main problems of agriculture that he faced were, first, how the proliferation of 'minuscule farms' and its negative effects were to be solved, and, second, how agriculture was to be developed in coordination with the growth of domestic industry. Further, in List's era the idea of developing into an industrial power capable of standing up to England by means of protectionist measures was beginning to emerge as a realistic objective.

A second reason for the difference between the two thinkers was the difference between their ideologies. For Müller, who subscribed to an ideal originating from the Middle Ages that ethical ties and economic developments should be united, the permeation of the whole of society with commercialism was in itself an extremely serious sign that 'we forget [the preeminence of] the personal over the material, being over having, the spirit of freedom over the brutish impulse of urgent need'. List, on the other hand, while also knowing that ethical and institutional relationships should not be ignored, adopted the standpoint of the growing industrial capitalists. He

found it gratifying that all branches of the national economy should grow to commercial maturity on the basis of industry, because this kind of maturing signified that the nation had at last reached the stage of the 'normal nation' [normalmäßige Nation] (List 1841:49, 210), a state that is able to compete with other developed states on even terms in world markets. List, in fact, attacked the ex-lords who had transformed themselves into large farmers because they hindered the 'reform of agriculture', i.e. the 'rounding of estates' (List 1842:451, 475–7).

Müller had doubts about the very nature of commercialization, but admitted that it might be suitable for the conditions in England. The burning question for him, however, was why mercantile agriculture, with all the risks it entailed, had to be imposed on Germany, especially in a top-down fashion, in the absence of the kind of conditions that existed in England. In his opinion, what Germany ought to be learning from England was not the spread of commercialism, but the 'inviolate sacred laws of the state' and the parliamentary system, both continuing naturally from the Middle Ages.[13] The functioning of the parliamentary system, for example, is one of the main reasons why England, in spite of its powerful commercialism, remained exempt from its negative effects.

When we consider arguments like this, it is obvious that Müller's view of 'true advances' differs from the classical Smithian view of 'general laws of development'. The Smithian view can be characterized, first, by the prospect of a general expansion of modern commerce and industry, together with mercantile agriculture, and, second, by the advance of natural development, without artificial policies. Although Müller was prepared to pursue the second of these characteristics in a form corresponding to the peculiarities of the German reality, he harbored doubts about the first one, especially from the non-commercialistic perspective of the old feudal nobility. He thought that in Germany, at least, rapid commercialization was not natural development and, if promoted, would have too many negative effects.

In this respect, we can understand Roscher's lower esteem for the later Müller after the publication of *Die Elemente der Staatskunst*. Müller's view of development had been already suggested to some extent in *Die Elemente,* but it did not become fully explicit until 'Agronomische Briefe', after which Müller continued to hold fast to it. Roscher was disappointed with this. In his own way, Roscher also attempted to pursue the second point of Smithian thinking on development, when he asserted that it proceeds 'through natural spiritual powers of men' according to 'natural laws' (Bücher 1894:106–7). He rated highly for Müller's criticisms of excessive materialism,[14] and wished to find a place for German peculiarities. But for all his sympathy for Müller on these aspects of the question, Roscher was unable to overlook a difference between England and Germany with respect to higher and lower stages of development. From this perspective, we can understand Roscher's

criticism that Müller, with his logic of contrast, only grasped differences between nations as a matter of parallelism, and that this led him to ignore the difference between stages of development. Roscher believed that Müller ought to have recognized the higher stage of England and the backwardness of Germany and should have been more conscious of Germany's need to catch up with England. Accordingly, Roscher not only adhered to Smith's principle of pursuing a natural course of development that took national peculiarities into account, but also attempted to observe Smith's first, commercialistic principle, too. In this respect, Roscher's standpoint was similar to that of List.[15]

The most notable feature of Müller's argument in 'Agronomische Briefe' is his view that cooperative relationships which have existed since the Middle Ages should be maintained, and that the development of trade and industry is not everything in a national economy. This cooperationalist view comes to the fore in his 1816 book *Versuche einer neuen Theorie des Geldes* [Attempts at a New Theory of Money], where he proposes to relieve poor citizens through the establishment of credit institutions possessing a superiority to savings banks. For Müller, credit systems of this kind are a way in which the medieval idea of cooperation can be newly realized in a society of growing commercialism.[16] After Müller's time, it was left to Bruno Hildebrand (1812–78) to advocate the establishment of credit systems and savings banks as a means of reviving the cooperative ideal of the past. In this respect, the viewpoint of Müller was carried on in the Older Historical School by Hildebrand rather than by Roscher, although Hildebrand, too, voiced certain critical opinions.[17]

Notes

1 Roscher (1843:iv–v); Tamura (1993:30–1); Schumpeter (1954:508); Priddat (1995:15–6).
2 Kobayashi (1990:65–6, 72–3, 75).
3 List (1842:423).
4 Kobayashi (1990:76–7; 1978:270–1). Here Kobayashi implies a path of continuity from Möser through List and Georg Hanssen to Richard Walter Darré, the minister of agriculture under Hitler.
5 Müller (1812:148–50); Lenz (1912:5–11, 93).
6 Müller (1809, half-vol. 1:276, half-vol. 2:22).
7 Knapp (1887, 2:233); Klein (1965:148–65).
8 Baxa (1930:167–9).
9 Huber (1957:136–45); Simon (1955:67–76). The Regulation Edict of 1811 was originally composed by Friedrich von Raumer, but the text was then considerably changed by nobles, who detected its 'excessive' concern for peasants' livelihood. After being redrafted to ensure the nobles' material interests, it was proclaimed as an edict. Knapp (1887, 1:162–71); Klein (1965: 148–51).
10 This assertion has characteristics similar to those assumed by the 'Older German School of Value in Use' [ältere deutsche Gebrauchswertschule], which was—strictly speaking—not a school but a value theory trend in Germany during the

nineteenth century. Komorzynski (1889:63–83); Spann (1969:199); Brandt (1992:169–84); Priddat (1997).
11 Baxa (1930:176–93, 217–9).
12 Müller (1809, half-vol. 1:302–5; Harada (1994:178–80).
13 On Müller's teaching on the parliamentary system with reference to that in England, see Müller (1810:160–3).
14 Roscher (1874:767).
15 But Roscher (1874:973–4) is critical of List's over-estimation of individual state measures and polemics against Smith and School in his Germany. Tamura (1993:30).
16 Müller (1816:145–6; 1819b; 1809, half-vol. 1:307–9).
17 Hildebrand (1864:21–3; 1848:278–9); Harada (1996).

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Chapter 3

A lecture notebook of Wilhelm Roscher with special reference to his published works

Yukihiro Ikeda

What is the significance of the lecture notes of an economist? Do they only strike the fancy of schizophrenic historians who are eager to know the details not only of economic doctrines but also of the personal lives of economists, such as those presented in Hession's (1984) fascinating biography of John Maynard Keynes? Or, rather, are they important materials for research and analysis to help us place these thinkers' positions in perspective? In considering the existing lecture notebooks of Adam Smith, Carl Menger, Eugen von Böhm-Bawerk, and Keynes himself, as well as the lecture notes prepared by Max Weber—to name only a few examples—I am of the latter opinion.[1]

Economic theories and economic discourse are communicated to others through various media, such as books, research papers, e-mails, face-to-face conversations, and classroom lectures. Inevitably, the contents of conversations fade almost as soon as they are over. Thus there is little oral evidence to tell us how economic discourse is diffused. Remarkable exceptions are the lecture notes prepared by academicians and the notes taken by students during the lectures. True, not all students are diligent note-takers. It is highly possible that a *détour* will not be written down, since it is not an essential part of the lecture. Or some portions of a lecture might have been skipped because the student was absentminded or bored. Nevertheless, it is safe to say that lecture notebooks do reflect at least the core of the lectures delivered in the classroom, especially in German-speaking areas, where professors usually read their well-prepared notes.

Another problem is the audience's basic understanding of the subject matter. Since almost all of the surviving materials relate to undergraduate students, we cannot expect them to contain the same level of argument that is found in the monographs. Still, lectures are important sources of the diffusion process of economic science: they show how the discipline is explained by teachers and how it is digested, accepted, and criticized by students. To be understood, teachers often must simplify their lectures and water down economic theories. But if we are concerned not only with elevated theories but also with how economic science has been

institutionalized, this process itself is of interest. Furthermore, if students are exceptional as in the case of Knut Wicksell, who attended the lectures of Carl Menger in Vienna, we can expect some kind of reaction from them.[2]

Introduction

This chapter presents a lecture notebook of Wilhelm Roscher (1817–1894), one of the founders of the German Historical School, who taught for many years at Leipzig University. When Roscher was appointed Professor of Practical State Sciences and Cameralistics in 1848, Leipzig was the third largest university in Germany, with an enrollment of 3,000 students, it was second only to Berlin and Munich.[3] Roscher was a successor of Georg Hanssen, a historian of agriculture, who is also reckoned to have been a member of the German Historical School. In Leipzig Roscher lectured on such topics as economic theory, economic policy, practical economics and economic policy, public finance, comparative statistics and the state of affairs in European states.[4] A representative list of his lectures includes:

Winter Semester, 1866–7
History of Political Theories
Practical Economics and Economic Policy
Public Finance

Winter Semester, 1874–5
General Economic Theory
History of Political and Social Theories
Seminar on the Cameralist Society

Winter Semester, 1877–8
Practical Economics and Economic Policy
Public Finance
Major Theories of Agricultural Policy and Statistics[5]

Roscher resigned his post in 1888. He was succeeded by Lujo Brentano, a representative player of the German Historical School. After Brentano's brief tenure, August von Miaskowski was appointed Professor of Economics in 1891. Another economics post was occupied by Karl Bücher in 1892.[6] Among the economics professors at Leipzig, we know that Roscher, Brentano, and Bücher belonged to the German Historical School, Roscher representing its early stage and Brentano and Bücher its later stage. If Klaus Hennings is correct in judging Hanssen to be a member of that school,[7] we can count four already.

To whom were Roscher's lectures given? Because students at that time were the elite of German society and belonged to what German historians call the *Bildungsbürgerturn* (middle-class intellectuals), one supposes that

the lectures were academic rather than practical in nature. In his classical work on the *Bildungsbürgertum,* Fritz Ringer (1990) describes the situation at Leipzig University as follows:

> Among fathers of students at the University of Leipzig, the representation of higher officials, jurists, professors, gymnasium teachers, clergymen, and doctors was almost 46 percent in 1859–1864 and still 31 percent in 1879–1884. Entrepreneurs and wholesale merchants moved from about 2 percent in the early 1860s to just above 5 percent in the early 1880s, while other merchants and innkeepers increased their share from about 11 percent to just under 20 percent during the same period.
>
> (Ringer 1990:41)

This description clearly shows that the *Bildungsbürgertum* was still dominant from the late 1850s to the early 1880s, while Roscher was at Leipzig. By adding the number of entrepreneurs and wholesale merchants to the number of other merchants and innkeepers, we can see that in the early 1880s only 16 percent of the students were from the mercantile and entrepreneur classes. Naturally one supposes that if Roscher's lectures had no practical concerns, they had nothing to do with business. Yet, Roscher emphasized that he wrote his book for businessmen and students, as the subtitle of his *System* shows. Curiously, his book was first of all for businessmen and only secondly for students.[8] What was his actual intention? Did he really want businessmen to read his text? To answer these questions we must turn to his lectures and find out what he said in the classroom. We are able to identify the details of Roscher's lectures from examining a lecture notebook compiled by one of his students. This document (hereafter cited as the Notebook), entitled 'Lectures on the State Economy by Wilhelm Roscher in Leipzig,' is now housed at Keio University in Japan. It consists of four parts:

1 Elementary Course [Anfangsgründe], Winter Semester, 1849–50, 48 pages.
2 General Statistics Using the Comparative Method [Allgemeine Statistik auf vergleichender Methode], date unknown, 48 pages (pages 42–8 are blank).
3 Economics [Volkswirthschaftslehre], 97 pages. First Part: Summer Semester, 1849, pp. 1–46. Second Part: Winter Semester, 1850–1, pp. 48–97. Page 97 is unpaginated; the left side of this page is the last part of the 'Economics,' and the right side is the front page of 'General Public Finance' (below).
4 General Public Finance [Die gesammte Finanzwissenschaft], Winter Semester, 1849–50, 36 pages. Page 36 is unpaginated; the left side of this page is the last part of the 'General Public Finance,' and the right side is the front page of the first appendix.

There are two appendices; the first has 36 pages, the second 20 pages. Thus, altogether this Notebook consists of 285 pages. The average length of each lecture is 40 pages, perhaps corresponding to the available hours in one semester. All the notes are handwritten in black ink. As is true of other lecture notebooks in German-speaking areas, one encounters abbreviations of various kinds, which can be easily transformed into complete words. In this chapter quotations from the Notebook remain intact, including abbreviations. The Notebook is a pure reproduction of Roscher's lectures in Leipzig, unannotated by the student who compiled it.

Since this notebook is based on his lectures at Leipzig in 1849–51, one can expect some similarities to Roscher's previous work, *Grundriss zu Vorlesungen über die Staatswirthschaft* [Outlines of Lectures on the State Economy; hereafter cited as *Grundriss*], a short book also written for his lectures and published in 1843. In this chapter we see the basic similarity between *Grundriss* and the theoretical part of Economics as the third part of the Notebook.

The Notebook also casts new light on the formation of Roscher's masterpiece, *System der Volkswirtschaft*. Roscher's *System* is known not only for being one of the influential textbooks in the latter part of the nineteenth century, but also for its lexicographic content: one must digest various economic concepts without understanding the relationships of the various doctrines that Roscher introduces. It seems that Roscher knows everything, but often one fails to ascertain his point. This characteristic of Roscherian economics is closely related to his basic attitude toward the discipline: 'economic practice which is obviously related to economic institutions and determined by the specific circumstances of time and place, determines economic thinking'. (Backhaus 1995:7).[9] Thus, as Mark Blaug and Jürgen Backhaus rightly point out, Roscherian economics is relativistic in nature.[10] Nevertheless, many economists in German-speaking areas used this textbook as students, among them Carl Menger, the founder of the Austrian School of Economics.[11] Compare the titles of the four parts of the Notebook with those of the five volumes of the *System*:

Vol. 1, Fundamentals of Economics [Grundlagen der Nationalönomie], 1st edn, 1854
Vol. 2, Economics of Agriculture [Nationalökonomik des Ackerbaues und der verwandten Urproduktionen], 1st edn, 1860
Vol. 3, Economics of Trade and Industry [Nationalökonomik des Handels und Gewerbfleißes], 1st edn, 1881
Vol. 4, System of Public Finance [System der Finanzwissenschaft], 1st edn,1886
Vol. 5, System of Poor Relief [System der Armenpflege und Armenpolitik], 1st edn, 1894.

As we shall see, the practical aspects of economics in the Notebook are closely related to the subsequent volumes of *System*. The title of the fourth part in the Notebook refers to the fourth volume of *System,* also called *Finanzwissenschaft*. Together with the fact that the Notebook covers the period 1849–51, this leads us to speculate that this document might be seen as a draft of *System*. Or in other words, the Notebook is presumably a halfway point between *Grundriss* and *System*.

The next section of this chapter is concerned with the essence of Roscherian economics and its influences. The third section deals with the relationship between *Grundriss* and the Notebook. The fourth and fifth sections demonstrate that *System* can be seen as a further development of Roscher's lectures in Leipzig.

Roscherian economics and its influences

As I indicated elsewhere, Roscherian economics is unthinkable without the influences of the English Classical School. However, this does not mean that Roscher accepted Ricardian labor theory of value totally, which assumed the free competition of entrepreneurs. Roscher treated this problem as an exception to the cost of production theory, but it is an important exception for Roscher. Roscher explains the crux of the matter as follows:

> The rule that goods with the same cost of production have also equal value in exchange, is applicable only to the extent that it is possible to transfer the factors of production at will from one branch of production to another.
>
> (Roscher 1882:328)

In this case the price level cannot be explained by the usual method:

> Thus, in the case of the works of art of a deceased artist, which cannot be increased in number; or in that of living celebrities who cannot extend their mental activity in the same degree as their reputation grew. So, also, in the case of precious stones, which are sometimes found free, and therefore cost nothing, but which, at the same time, have a high price.
>
> (Roscher 1882:329)

Concerning this kind of anomaly there were three possible answers in the history of economic thought: the first was given by David Ricardo. He had acknowledged the above examples of the works of an artist and thought that these examples constituted a small portion of the whole commodities. Hence, *de facto,* he decided to ignore them. Roscher represented the second answer. For him, the above examples cannot be underestimated, but are

still compatible with the labor theory of value. In the above quotation, Roscher went as far as to say that precious stones cost nothing, but that they are still valuable. As we know, this statement can lead to the breakdown of the whole system of the English Classical School. But Roscher writes that 'Ricardo's doctrine is more tenable than appears at first blush' (Roscher 1882:320) in the thirteenth edition of *Grundlagen,* a statement which cannot be found in the works of the three stars of the Marginal Revolution. Obviously Roscher did not want to discard the English Classical School. This shows his eclectic method clearly, separating him from true antagonists of that school. The third answer was given by the representative scholars of the Marginal Revolution, Carl Menger and William Stanley Jevons. For them, the above-mentioned anomaly was not compatible with the value theory of the English Classical School. They tried to construct a unified value theory, starting from the preferences of consumers, which enabled them to explain the above cases without making them exceptions to the principle.

Since John Stuart Mill's *Principles of Political Economy* was published in 1848, we have to interpret the above statement of Roscher by considering the former's influences. Mill discussed the cases of commodities which cannot be multiplied by human powers.[12] This corresponds to the case of works of an artist in the above quotation from Roscher's *Grundlagen.* However, Mill and Roscher were not of the opinion that these cases would lead to the collapse of Ricardian economics. On the contrary, they tried to maintain the tradition of the English Classical School. Another possibility was provided by Karl Heinrich Rau, also a representative textbook writer in the nineteenth century. In *Grundsätze der Volkswirtschaftslehre,* Rau indicated the above example of works of an artist as an important exception to the cost of production theory. Since the first edition of Rau's work was published in 1826, we may draw the line Rau-Mill-Roscher, concerning the important exceptions to Ricardian orthodoxy. Anyway, Roscher's attitude to the English Classical School is obvious:

> We need only to interline his theory of rent, admit that capital is accumulated labor, subtract all objects constituting a natural monopoly, and not forget that the intrinsic value of labor is one of the causes of the difference of price of different sorts of labour.
>
> (Roscher 1882:320)

Roscherian economics was well-known in the nineteenth century. Karl Marx describes the essence of Roscherian economics as follows:

> But Bastiat does not represent the last stage. He is still marked by a lack of erudition and a quite superficial acquaintance with the branch of learning which he prettifies in the interests of the ruling class. His

> apologetics are still written with enthusiasm and constitute his real work, for he borrows the economic content from others just as it suits his purpose. The last form is the *academic form,* which proceeds 'historically' and, with wise moderation, collects the 'best' from all sources, and in doing this contradictions do not matter; on the contrary, what matters is comprehensiveness… Professor Roscher is a master of this sort of thing and has modestly proclaimed himself to be the Thucydides of political economy.
>
> (Marx 1971:502)

This quotation from the *Theories of Surplus-Value* aptly captures the essence of Roscherian economics. Marx classifies what he calls vulgar economics into two stages in the above quotation: one represented by Frédéric Bastiat, a well-known French economist, and the other by Roscher. Although both belong to the vulgar economics, Marx regards their opinions of capitalism as totally different. Bastiat still has a passion for capitalism; for this reason Bastiat is located in the earlier stage of vulgar economics. Roscher's standpoint is different. He is indifferent to various economic doctrines; his economics is relativistic in nature. Thus, Roscherian economics degenerated into what Marx called the 'the last stage' of vulgar economics. This characterization of Roscherian economics corresponds to our description in the previous section.

To see another example of Roscher's influences, we now turn to Carl Menger, the founder of the Austrian School of Economics. As the previous scholarship has already shown, Menger studied Roscher's textbook very seriously in the 1860s. Here we deal with his lectures to Prince Rudolf in the 1870s. The following explanation of the merits of division of labor is Menger's:

> The resulting virtuosity of the individual worker… Saving of time and effort… International division of labor through which a country imports the products of foreign countries; each country pursues its specific activities, and then trades with the other countries.[13]
>
> (Menger 1994:39, 41)

As Erich Streissler rightly pointed out,[14] we find almost the same argument in Roscher's *Grundlagen.* Roscher's explanation runs as follows:

> Bigger virtuosity of worker… Enormous saving of time and effort… As the land is a natural extension of national organism, international division of labour offers an indirect, but often only method to obtain products of foreign regions and climate.[15]
>
> (Roscher 1883:126–8)

These two examples show that Roscher was influential from the early 1860s to the late 1870s. Marx and Menger, two completely different economists, read Roscher eagerly, of course not without criticism, and sometimes disparagingly as in the case of Marx.

Grundriss and the lecture notebook

First, let us look at the structure of the Notebook and *Grundriss*. With regard to the Notebook, we concentrate on the first part of Economics, which consists of three books. The contents of Book 1 are as follows (here and elsewhere in this chapter the first parenthesis gives the German title, and the second denotes its relationship with Roscher's published works):

Book 1: General Part [Allgemeiner Theil] (*Grundriss,* Book 1, also entitled Allgemeiner Theil)

Chapter 1: Production [Production] (*Grundriss,* Book 1, Chapter 1, Erzeugung der Güter)

1 Factors of Production [Factoren der Gütererzeugung] (*Grundriss,* Book 1, Chapter 1, Section 5, entitled Factoren der Gütererzeugung)
2 Division and Combination of Labor [Theilung und Vereinigung der Arbeit] (*Grundriss,* Book 1, Chapter 1, Section 6, entitled Theilung und Vereinigung der Arbeit)
3 Productivity of Various Workers [Productivität der verschiedenen Arbeiter] (*Grundriss,* Book 1, Chapter 1, Section 7, entitled Productivität der verschiedenen Arbeiten)
4 Personal Freedom [Persönliche Freiheit]
5 Property [Eigenthum] (*Grundriss,* Book 1, Chapter 1, Section 5–5. Eigenthum)
6 Credit [Credit] (*Grundriss,* Book 1, Chapter 2, Section 9–4. Credit)

Chapter 2: Distribution of Goods [Vertheilung der Güter] (Second chapter of *Grundriss,* also entitled Vertheilung der Güter)

7 Price in General [Preis im Allgemeinen] (*Grundriss,* Book 1, Chapter 2, Section 8, entitled Bestimmung des Preises im Allgemeinen)
8 Money in General [Geld im Allgemeinen] (*Grundriss,* Book 1, Chapter 2, Section 9, entitled Geld und Credit im Allgemeinen)
9 History of Price [Geschichte der Preise] (*Grundriss,* Book 1, Chapter 2, Section 10, also entitled Geschichte der Preise)
10 Income in General [Einkommen im Allgemeinen] (*Grundriss,* Book 1, Chapter 2, Section 11, entitled Einkommen)
11 Rent [Grundrente] (*Grundriss,* Book 1, Chapter 2, Section 12, also entitled Grundrente)

12 Wage [Arbeitslohn] (*Grundriss,* Book 1, Chapter 2, Section 13, also entitled Arbeitslohn)
13 Interest on Capital [Capitalzins] (*Grundriss,* Book 1, Chapter 2, Section 14, also entitled Kapitalzins)
14 Concluding Remarks on Income [Schlußbetrachtungen über das Einkommen]

Chapter 3: Consumption [Consumtion] (Book 1, Chapter 3 of *Grundriss,* entitled Verzehrung der Güter)

15 Consumption in General [Consumtion im Allgemeinen] (*Grundriss,* Book 1, Chapter 3, Section 16, also entitled Consumtion im Allgemeinen)
16 Luxury [Luxus] (*Grundriss,* Book 1, Chapter 3, Section 17, also entitled Luxus)
17 Appendix: Population in General [Bevölkerung im Allgemeinen] (*Grundriss,* Book 2, Chapter 4, Section 42, also entitled Bevölkerung im Allgemeinen)

In the first part of Economics, Book 1 entitled General Part corresponds to the first book of *Grundriss,* also entitled General Part. Of the seventeen sections of the General Part of the Notebook, fourteen are based on *Grundriss*. Sections 1–6 correspond to Book 1, Chapter 1, Sections 7–14, to Chapter 2 of *Grundriss*. And the following two sections, Sections 15–16, in the Notebook are related to Book 1, Chapter 3 of *Grundriss*. In these sections the order in *Grundriss* is generally the same: both *Grundriss* and the Notebook begin with the production of goods, followed by the distribution of goods and the consumption of goods. Lastly, in Section 17 as an appendix Roscher teaches his students population theory, which finds its counterpart in Book 2, Chapter 4, not in Book 1. The peculiar position of population shows Roscher's later idea that population theory can be integrated with economic theories. In fact, he followed this procedure in the first volume of *System,* beginning with the production of goods and ending with population theory.

The remaining lectures which are devoted to topics such as agriculture and trade, rely heavily on *Grundriss*. In the last part of the Notebook Roscher gives detailed information on the literature. The contents of Book 2 of the Notebook are as follows:

Book 2: Branches of Economics [Die Zweige der Volkswirthschaft im besonderen]

Chapter 1: Agriculture [Urproduction]

1 Hunting and Fishing [Jagd und Fischerei] (*Grundriss*, Book 2, Chapter 1, Section 18, also entitled Jagd und Fischerei)

2 Livestock Production [Viehzucht] (*Grundriss,* Book 2, Chapter 1, Section 19, also entitled Viehzucht)
3 Theory and History of the Field System [Theorie und Geschichte der Feldsysteme] (*Grundriss,* Book 2, Chapter 1, Section 22, also entitled Theorie und Geschichte der Feldsysteme)
4 Social Relationship of Agriculture [Sociale Verhältnisse der Landwirthschaft]
5 Economics of Forestry [Forstwirthschaft] (*Grundriss,* Book 2, Chapter 1. Section 28, also entitled Forstwirthschaft)
6 Mining Expansion Policy [Bergbau] (*Grundriss,* Book 2, Chapter 1, Section 29, also entitled Bergbau)

Chapter 2: Industry [Gewerbfleiß] (*Grundriss,* Book 2, Chapter 2, entitled Gewerbfleiß)

7 Industry in General [Gewerbfleiß im Allgemeinen]
8 Handicrafts, Manufacturing and Factories [Handwerk, Manufaktur und Fabrik]
9 System of Machinery [Machinenwesen]

Chapter 3: Trade [Handel] (*Grundriss,* Book 2, Chapter 3, also entitled Handel)

10 Trade in General [Handel im Allgemeinen]
11 International Trade [Internationaler Handel]
12 System of Coinage and Banks [Münz=u. Bankwesen] (*Grundriss, B*ook 2, Chapter 3, Section 38, entitled Geld=und Bankwesen)
13 Means of Communication in General [Communicationsmittel im Allgemeinen]
14 Appendix [Anhang]

Sections 1–6, Book 2 of the Notebook are based on Book 2, Chapter 1 of *Grundriss*. This part is considered to be agricultural economics. Sections 7–14, which are devoted to industry and trade, correspond to Book 2, Chapters 2 and 3 of *Grundriss*. Book 3 of *Grundriss* was concerned with public finance, but in the Notebook this topic is not included in the Economics part, but in the separate General Public Finance part. Roscher goes directly to the discussion of the literature on the subject in Book 3:

Book 3: History of the Literature [Litterärgeschichte] *(Grundriss,* Book 4, also entitled Literärgeschichte)

1 Ancient Times [Alterthum] (*Grundriss,* Book 4, Section 56, also entitled Alterthum)
2 Mercantile System [Merkantilsystem] (*Grundriss,* Book 4, Section 57, also entitled Mercantilsystem)

3 Reaction against the Mercantile System [Reaction gegen das Merkantilsystem] (*Grundriss*, Book 4, Section 58, also entitled Reaction gegen das Mercantilsystem)
4 Adam Smith, His Pupils and Successors [Adam Smith, seine Schüler und Nachfolger] (*Grundriss*, Book 4, Section 59, also entitled Adam Smith, seine Schüler und Nachfolger)
5 Reaction against Adam Smith [Reaction gegen Adam Smith] (*Grundriss*, Book 4, Section 60, also entitled Reaction gegen Adam Smith)

Book 3 of the Notebook strictly corresponds to Sections 56–60 of *Grundriss*. All the section titles find their exact equivalence in *Grundriss*. A glance at the table of contents leads us to conjecture that Roscher in fact read *Grundriss* in the classroom. Six years earlier he had published *Grundriss* for his lectures at Göttingen University, but the main arguments did not seem to change as far as the theoretical part of Economics was concerned.

Next we turn to the details of the Notebook. The introductory part of Economics consists of the following sections:

- Method of State Science in General [Methode der Staatswissenschaft im Allgemeinen]
- Objective of the National Economy [Gegenstand der Nationalökonomie]
- Position of the National Economy in the Circle of State Sciences and Cameralistics [Stellung der Nationalökonomie im Kreise der Staats- u. Kammeralwissenschaften]

This is almost the same as the introductory part of *Grundriss*:

- Method of State Sciences in General [Methode der Staatswissenschaften überhaupt]
- Objectives of the State Economy [Gegenstände der Staatswirthschaft]
- Position of the State Economy in the Circle of Other Political Sciences [Stellung der Staatswirthschaft im Kreise der übrigen politischen Wissenschaften]

In *Grundriss* Roscher uses a concept of 'State Sciences' as well as 'State Economies', whereas in the Notebook one finds phrases like 'National Economies', a very traditional terminology in German economics. This concept does not appear in the foregoing quotation from *Grundriss*. Apart from this small difference in the terminology, the two quotations are the same.

Regarding substance, many sentences in the Notebook are almost identical to those in *Grundriss*. For instance, in the introductory part of Economics Roscher defines goods:

> Goods are anything which can be used for the satisfaction of any human need, and whose utility for this purpose is recognized. With the development of culture the scope of the goods is enlarged automatically. Exchange lies in the bilateral human needs. A continuous relationship through bilateral services is called circulation. Our science deals with only those goods which circulate.[16]
>
> (Roscher 1849–51:6.l–6.r)

This is almost exactly what we find in *Grundriss*, where he says:

> Goods are anything which can be used for the satisfaction of any human need, and whose utility for this purpose is recognized. Relativity of this concept. With the development of culture the scope of the goods is enlarged automatically. Exchange lies in the bilateral human needs. A continuous relationship through bilateral services is called circulation. Our science deals with only those goods which circulate, that is, only economic goods.[17]
>
> (Roscher 1843:2–3)

There are slight differences in these quotations. The brief phrase in *Grundriss*, 'Relativity of this concept' does not appear in the Notebook, nor does 'only economic goods' in the last part of the second quotation. In the Notebook the definition of goods is followed by basic concepts, such as value, property, wealth, and economy, an approach also taken in *Grundriss*.

Another similarity of the two works is in the treatment of price theory. The following sentences are taken from the Notebook:

> Price. Price is the exchange value of a good, expressed in the volume of other goods which are exchanged for it. Every price decision is made by the conflict of interests. The seller tries to attain a high price from the buyer, the buyer a possible low price from the seller. Thus, the decisive moment is the relationship between demand and supply.[18]
>
> (Roscher 1849–51:11.r)

After defining price as the exchange value of a commodity, Roscher goes on to describe the conflict between sellers and buyers. The seller tries to sell at the highest price, while the buyer seeks the lowest. In the end Roscher commits to the general statement often made by economists that 'the decisive moment is the relationship between demand and supply'. These sentences, including the last one, are exactly what we find in *Grundriss*, Book 1, Chapter 2, Section 8:

> Price is the exchange value of a good, expressed in the volume of other goods which are exchanged for it.... Every price decision is made by

> the conflict of interests. The seller tries to attain a high price from the buyer, the buyer a possible low price from the seller. Thus, the decisive moment is the relationship between demand and supply.[19]
>
> (Roscher 1843:10)

In *Grundriss* there is a short digression on the concept of *kostbar* and *theuer,* which I omitted from the quotation. Apart from this omission, these two quotations are the same. In this case Roscher followed his explanation in *Grundriss* almost to the word in his lectures in Leipzig. This again leads us to the conjecture that Roscher in fact read *Grundriss* in the classroom.

Grundlagen and the lecture notebook

As suggested earlier, these lectures include some hints of concepts to be developed in *System* years later. In Book 1, Section 5 of the Notebook, entitled *Eigenthum,* Roscher explains the conditions under which socialism is possible and why it breaks down:

> So far as the parts are integrated with the spirit of true love, the society could be perhaps sustainable. Otherwise because of self-love, which permeates the very nature of human beings, an unavoidable result would be that every participant produces as little as possible and consumes as much as possible. General poverty, savagery and namely overpopulation.[20]
>
> (Roscher 1849–51:10.1)

Roscher believes that socialism will necessarily collapse unless the participants are strictly bound up with other members of the society. Since it is possible under this system to get as much as possible without working hard, GDP or GDP per man will decline. This is, in a nutshell, the reason why socialism will not work. We find almost the same argument in *Grundriss,* Book 1, Chapter 1, Section 5, also entitled *Eigenthum:*

> So far as the number of participants is small and so far as they have a sacrificing spirit of religious enthusiasm, the society would be sustainable. Otherwise because of self-love, which permeates the very nature of human beings, an unavoidable result would be that every participant works as little as possible and consumes as much as possible.[21]
>
> (Roscher 1843:7–8)

Considering these two quotations, it is certain that Roscher's lectures are still based on *Grundriss.* However, one finds in the Notebook sentences that are similar to those in *Grundlagen,* the first volume of Roscher's *System.* For instance, in his lectures Roscher says that socialism is compatible with lower stages of economic development. We cannot find the following sentence from

the Notebook in *Grundriss,* Book 1, Chapter 1, Section 5: 'By the way, we find in history that the rudest and poorest cultural stages began with a more or less associative character'. (Roscher 1849–51:10.r).[22] This sentence finds its echo in Roscher's later work, namely *Grundlagen*: 'By the way, from experience we know that in most cases very poor and rude cultural stages have a more or less associative character' (Roscher 1883: 192).[23] Apart from the minor difference in terminology, these two quotations are basically the same.

Subsequent volumes of System and the lecture notebook

The third part of the Notebook, Economics, consists of two subparts: theoretical and practical. The previous section was concerned with the theoretical part and its relationship with *Grundriss*. Listed below are the contents of the practical part of Economics and its relationship to *Grundriss* and *System*. As before, the first parenthesis gives the original German title, and the second denotes its relationship to Roscher's published works:

1 Formation of State Power in Conflict with Small Juridical Persons [Ausbildung der Staatsgewalt im Kampfe mit den kleinen juristischen Personen] (*Grundriss,* Book 2, Chapter 1, Section 20, also entitled Ausbildung der Staatsgewalt im Kampfe mit den kleinen juristischen Personen)
2 History of Agricultural Classes [Geschichte der landbauenden Classen] (*Grundriss,* Book 2, Chapter 1, Section 21, also entitled Geschichte der landbauenden Klassen)
3 The Relation of Landed Property to the Family [Verhältnisse des Grundeigenthums zur Familie] (*Nationalökonomik des Ackerbaues,* Section 88)
4 The Relation of Landed Property to the Municipality [Verhältnisse des Grundeigenthums zur Gemeinde] (*Nationalökonomik des Ackerbaues,* Section 71, entitled Das Grundeigenthum und die Gemeinden)
5 Real Burden [Reallasten]
6 Real Credit [Realcredit] (*Grundriss,* Book 2, Chapter 1, Section 26, also entitled Realcredit)
7 Corn Trade and Price Increase Policy [Kornhandel und Theuerungspolizei] (*Nationalökonomik des Ackerbaues,* Sections 150–1, entitled Kornhandel und Theuerungspolitik)
8 Forestry Police [Forstpolizei]
9 Mine Security Police [Bergpolizei]
10 History of Cities [Geschichte des Städtewesens]
11 Privilege and Rights of the Guild [Bann und Zunftrechte]
12 Constraints on Trade in the Middle Ages [Handelsbeschränkungen des Mittelalters]

13 Freedom of Industry [Gewerbefreiheit] (*Grundriss,* Book 2, Chapter 2, Section 33, also entitled Gewerbefreiheit)
14 The Protective System and Freedom of Trade [Schützsystem und Handelsfreiheit]
15 System of Communication [Communicationsanstalten] (*Grundriss,* Book 2, Chapter 3, Section 40, also entitled Communicationsanstalten)
16 Production Crisis [Productionskrisen] (*Grundriss,* Book 2, Chapter 3, Section 39, also entitled Productionskrisen)
17 Colonial Policy [Kolonialpolitik]
18 History of Pauperism [Geschichte des Pauperismus]
19 Poor Relief Policy in General [Armenpolitik im Allgemeinen]
20 Further Observations on Individual Poorhouses [Nähere Betrachtung der einzelnen Armenanstalten](Grundriss, Book 2, Chapter 4, Section 44, entitled Nähere Beleuchtung der einzelnen Armenanstalten)

Here we can ascertain that the remaining lectures are at least partially based on *Grundriss*. Of the twenty sections in the practical part of Economics we find at least seven titles that correspond to those in the second book of *Grundriss*. Thus Book 2 of *Grundriss* finds its counterpart not only in the theoretical part but also in the practical part of Economics. Related topics appear in both lectures. At the same time these lectures were to be developed into *System* in later years, as the remarks in the parenthesis show. Section 3, for instance, corresponds to Section 88 of *Nationalökonomik des Ackerbaues,* entitled 'Das Grundeigenthum und die Familien'. Similarly Section 4 finds its counterpart in Section 71 of *Nationalökonomik des Ackerbaues* and Section 7 in Sections 150–1 of the same work, with a slight difference in the titles.

Concluding remarks

In this chapter, after briefly mentioning Roscher's position in the history of economic thought, we introduced the main content of the Notebook, now housed at Keio University. Roscher's Notebook is closely related to his previous work, *Grundriss*. In the third section we scrutinized the relationship between the first part of Economics and *Grundriss*. In some of his lectures in Leipzig Roscher repeated what he had written several years earlier in *Grundriss*. This is not surprising given the fact that *Grundriss* was also written for his lectures in Göttingen. In the latter part of this chapter an attempt has been made to find the roots of *System* in the lectures in Leipzig. In the fourth section it was demonstrated that a part of the Notebook finds its counterpart in *Grundlagen,* the first volume of *System*. The previous section concerned itself with the relationship between the Notebook and the subsequent volumes of *System*. Thus I hypothesize that the Notebook was a stepping stone to *System*. *System* came out of

Roscher's lectures at Leipzig. Although this conjecture remains a hypothesis here, his lectures in Leipzig will prove to be a germ of *System*, provided that we can find another set of lecture notebooks in the future.

Notes

1 See Menger (1993, 1994), Böhm-Bawerk (1998), Weber (1990), and Rymes (1989).
2 For a detailed explanation, see Tomo (1996). According to Tomo, Wicksell attended Menger's lecture on public finance in the summer session of 1888.
3 See Hennings (1988:122); Prahl (1978: table 3).
4 This information is based on Hennings (1988:144–6).
5 Hennings (1988:160–1).
6 Hennings (1988:145ff, esp. table 1).
7 Hennings (1988:144).
8 This curiosity is pointed out by Hennings (1988:145, n. 92).
9 Now it is generally recognized that Roscher in a sense was a follower of the English Classical School. See Betz (1988) and Eisermann (1992). For a detailed explanation of the relationship between Roscher and the English Classical School, see Ikeda (1995b). Streissler (1994, 1995) emphasizes that Roscher, besides being a founder of the German Historical School, was also good at economic theories.
10 Blaug (1985:3–4), Backhaus (1995:7). See also Backhaus (1992). Baltzarek (1994) also emphasizes the encyclopedic character of Roscherian economics.
11 For the relationship between Menger and Roscher, especially from the vantage point of the formation of Menger's *Grundsätze der Volkswirtschaftslehre*, see Ikeda (1995b, 1997), Streissler (1990a, 1990b), and Yagi (1993).
12 For a succinct explanation see Hollander (1987:124).
13 Original text: 'Die Erlangung großer Virtuosität der einzelnen Arbeiter… Ersparnisse von Zeit und Mühe… Die internationale Arbeitsteilung, durch welche die Produkte fremder Länder ins Inland gelangen können und jedes Land seine spezifischen Arbeiten verrichtet und sie dann den anderen Länder verhandelt' (Menger 1994:38, 40).
14 This indication is due to Streissler. See Menger (1994:38, n. 18). See also the editor's introduction included in Menger (1994).
15 Original text: 'Größere Virtuosität der Arbeiter…Einer Menge von Ersparnissen an Zeit und Mühe…. Wie das Land gleichsam die natürliche Erweiterung des Volksleibes ist, so bietet insbesondere die internationale Arbeitsteilung das zwar nur indirecte, aber oft einzige Mittel dar, sich die Erzeugnisse fremder Gegenden und Klimate zu verschaffen' (Roscher 1883:126–28).
16 Original text: 'Güter nennen wir alles dasjenige, was zur Befriedigung menschlicher Bedürfnisse anerkannt brauchbar ist. Mit dem Fortschreiten der Cultur erweitert sich der Bereich der Güter von selbst. In der wechselseitigen Bedürftigkeit der Menschen liegt der Tausch begründet. Eine fortgesetzte Verbindung durch wechselseitige Leistungen nennen wir Verkehr. Unsere Wissenschaft handelt nur von solchen Gütern, die in den Verkehr kommen.' (Roscher 1849–51:6.l–6.r). (This means that the quotation runs from left to right on p. 6; hereafter the same rule applies.)
17 Original text: 'Güter nennen wir alles dasjenige, was zur Befriedigung menschlicher Bedürfnisse anerkannt brauchbar ist. Relativität dieses Begriffes. Mit dem Fortschreiten der Kultur erweitert sich der Bereich der Güter von selbst.

In der wechselseitigen Bedürftigkeit der Menschen liegt der Tausch begründet. Eine fortgesetzte Verbindung durch wechselseitige Leistungen nennen wir Verkehr. Unsere Wissenschaft handelt nur von solchen Gütern, die in den Verkehr kommen, nur von wirthschaftlichen Gütern' (Roscher 1843:2–3).

18 Original text: 'Preis. Preis ist der Tauschwerth eines Gutes, ausgedrückt in dem Quantum eines bestimmten andern Gutes, das dafür eingekauft wird. Jede Preisbestimmung kommt durch den Kampf entgegengesetzter Interessen zu Stande. Der Verkäufer wünscht sich Käufer möglichst hohen, der Käufer wünscht sich Verkäufer zu möglichst niedrigen Preisen. Das entscheidende Moment also ist das Verhältniß von Angebot u. (und) Nachfrage' (Roscher 1849–51:11.r).

19 Original text: 'Preis ist der Tauschwerth eines Gutes, ausgedrückt in dem Quantum eines bestimmten andern Gutes, das dafür eingetauscht werden soll…Jede Preisbestimmung kommt durch den Kampf entgegengesetzter Interessen zu Stande: der Verkäufer wünscht sich Käufer zu möglichst hohen, der Käufer wünscht sich Verkäufer zu möglichst niedrigen Preisen. Das entscheidende Moment also ist das Verhältniß von Angebot und Nachfrage' (Roscher 1843:10).

20 Original text: 'So lange die Theile durch den Geist wahrer Liebe verbunden sind, würde die Gemeinsch. (Gemeinschaft) wohl bestehen künnen, sonst ab. (aber) müßte sie bei d. (dem) angeborenen Eigennutze der mensch. (menschlichen) Natur unvermeidlich zur Folge haben, daß jeder Theilnehmer möglichst wenig produciren, möglichst viel consumiren würde, also allgem. (allgemeine) Armuth, Rohheit u. (und) namentl. (namentlich) Uebervölkerung' (Roscher 1849–51:10.1).

21 Original text: 'So lange die Theilnehmer gering an Zahl und von dem aufopfernden Geiste eines religiösen Enthusiasmus beseelt sind, kann die Gemeinschaft füglich bestehen. Sonst aber würde sie, bei dem angebornen Eigennutze der menschlichen Natur, unvermeidlich zur Folge haben, daß jeder Theilnehmer möglichst wenig arbeiten, möglichst viel verzehren wollte' (Roscher 1843:7–8).

22 Original text: 'Wir finden übrigens in der Geschichte, daß die allerrohsten u. (und) ärmsten Culturstufen mit mehr od. (oder) weniger ausgebildeter Gütergemeinschaft angefangen haben' (Roscher 1849–51:10.r). Compare the following sentence in the Notebook with the one in *Grundlagen*: Notebook: 'In demselben Verhältnisse, wie sich darnach Bildung Wohlstand entwickelten, pflegte sich zugleich als Ursache u. Wirkung das Privateigenthum immer schärfer auszubilden.' (Roscher 1849–51:10.r). *Grundlagen*: 'Erst in demselben Verhältnisse, wie sich hernach der Wohlstand und die Bildung entwickelten, pflegte sich zugleich, als Wirkung und Ursache, das Privateigenthum schärfer auszubilden' (Roscher 1883:192).

23 Original text: 'Uebrigens lehrt die Erfahrung, daß die meisten sehr armen und rohen Kulturstufen wirklich mehr oder weniger Gütergemeinschaft haben' (Roscher 1883:192).

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Chapter 4

Karl Knies's conception of political economy

The logical status of *Analogie* and Sitte

Jun Kobayashi

The task of this chapter is to discern the problematic of the German Historical School, the concept of political economy in nineteenth-century Germany, and to discuss how this problematic has been treated in successive years. Although political economy became purified as economics or pure theory in the second half of the century, the German Historical School seems to have been left behind in this process. The main focus of this school was not on the development of analytic tools for market mechanisms, and that is why it seems to have become outdated from a retrospective viewpoint. How, then, did the German Historical School regard political economy? What were its theoretical problems? In considering these problems, we must first understand the school's characteristics. Here I am following the conventional conception of the old (Wilhelm Roscher, Bruno Hildebrand, Karl Knies) and the new school (epitomized by Gustav Schmoller).[1] To discern the school's characteristics and the shift within the school, I will examine Knies's idea of political economy with reference to the following two points.

1. Keith Tribe (1998) argues that the historicization of political economy in Great Britain produced economic history. For Germany, in contrast, the development was 'from historism to sociology' according to Carlo Antoni (1959).[2] Admitting the validity of these schemata, we will examine the role that Knies played in this process.
2. In 'Roscher und Knies', Max Weber's (1975:199–207) comments on Knies are intended to be a fundamental criticism of the tradition of German political economy. I would like to clarify in what sense Weber's criticism can be interpreted as going beyond the Historical School. At the end of this chapter I will make some observations about Wilhelm Hennis's work, which in a sense leaves the problematic of the Historical School alone and stresses the continuity between that school and Weber.

Knies's *Politische Oekonomie vom geschichtlichen Standpuncte* has been critically discussed in the history of economics, especially concerning its

conceptions of *Volk* (people) and developmental law, and for good reason.[3] But analysis of these words sometimes focused on the role of historicism and historical consciousness in the history of German ideas, and so could not present us with an effective frame of reference for the history of economic thought.

The reason why the German Historical School, especially the work of Knies, is not often mentioned in the history of economic thought may be that the economists in this school seemed to contribute little to theoretical progress. Knies gave political economy a normative character, and, as a consequence, later studies of his work, emphasized a series of historic-philosophical and intellectual-historical factors to prove the validity of such normativeness. This may also have contributed to the hostile attitude towards Knies. A recent study regards *Das Geld* as his main work from the viewpoint of its theoretical contribution (Häuser 1996:32–3). But if we are to discern his conception of political economy, then *Politische Oekonomie vom geschichtlichen Standpuncte* is indeed the most appropriate work. In dealing with this book, I will discuss the problematic of Knies and of German economic thought of the nineteenth century, symbolizing it with the words *Analogie* and *Sitte*.

Basic character of Knies's political economy

The first edition of Knies's book, *Politische Oekonomie vom Standpunkt der geschichtlichen Methode* (1853), was written as a methodological work. Knies himself stressed this point, and this was not changed as indicated in the preface to the second edition, published in 1883 under the new title *Politische Oekonomie vom geschichtlichen Standpuncte*.[4] His starting point is a critical examination of Roscher's 'historical method',[5] and he intended to improve it. Roscher used the term 'historical method' in an unusual way, Knies notes, not as a method to reach a conclusion but rather to provide the national economy with a historical description (Knies 1883:34–5).

Making reference to the label 'political economy', Knies first states that he will treat not mere theory, but 'political' economy, whose object he defines as 'human action and activity, and the socially and legally ordered condition of a life-community of individuals and total nation grounded through such action and activity' (1883:6). This object of reflection is not 'the world of thoughts and ideas of the inner man, but processes and conditions to be found in the world with perceptible appearances.' But an investigation into the causes of these external phenomena 'leads back to the spiritual sphere of the human interior'. In this way he establishes, to use a contemporary expression regarding the distinction of sciences, a third sphere between natural and spiritual science.

'At stake here is thus neither an "inner" nor an "outer" human world. Instead, we are concerned with a perceptible "outer-world" of phenomena

conditioned by "inner-worldly" causation and therefore not entirely accessible through the methods of natural-scientific research' (p. 7). Because of this dual character inherent in the object, political economy became involved in specific methodological difficulties. According to Knies, natural-scientific theory, which finds validity only in the outer world, has by now ascribed scientific absolutism to itself. This absolutism consists of two elements: cosmopolitanism and perpetualism (p. 24). His relativist critique conceives these elements as its target. So he starts with a critique of absolutism of natural-scientific theory. And he depicts the specific character of political economy:

> The economic life of a people is so closely interwoven with other areas of its life that any particular observation can only be made if one keeps in view its relation with the whole, existing as a truth in the complexity of empirical reality.
>
> (Knies 1883:436)

Stressing in this way the relationship of economic life with other areas and the continuity of generations in the total life of a people, Knies describes the nature of this discipline as follows:

> Since political economy has to respect this context, and in its own concerns contributes to the solution of the moral-political problems of the whole, it is therefore enjoined to take its place with the moral and political sciences. Only then does it effect a proper connection with real life, for in fact the individual as well as entire peoples and states seek to realize the objectives of their whole life through economic endeavor and economic success. In this way economic concern for material goods attains this level of political and ethical activity.
>
> (Knies 1883:436f.)

Analogie

Knies's antagonism towards natural-scientific theory is exemplified in his criticism of the theory, or of the English Classical School:

> The instinctive drive towards private interest of the individual is grasped as natural law, as parallel to the other laws that dominate the area of commodity. In the face of economic difficulties and disasters of individuals or of each class in society, the theory of national economy, supported by determinism and fatalism, tends to show that humans will lose their jobs under the pressure of the natural law that dominates the real world, even if it seeks to form its own ends and to set in motion ethical freedom and power. Or any theoretical

> statement on present conditions turns out to be an enthusiastic apologism. This basic tenor of the English school, regarding the natural law in the world of objective things as valid and complete everywhere, misunderstanding or discrediting the quality and the power of ethical freedom in human activities, and disregarding the significance of the concrete, individual and relative in opposition to the same, general and absolute, seeks to declare the invalidity of the human effort with free power against the almighty natural law, and to lead to the belief in the righteousness of an abstract formula made of truth taken out of concrete historical life.
>
> (Knies 1883:318–19)

Knies also admits that science in general aims to acquire not merely knowledge but laws of phenomena (p. 349). The problem is where to find 'the significance and nature of national economic law' (p. 349). As seen above, the real appearance of economic phenomena is conditioned by the fact that human actions are intimately connected with objective products and factors of an external nature (p. 351). The latter is subjected to natural law. But this law is not a law of national economy, but a law that appears in national economic phenomena, and is to be counted among economic activities (p. 352).

Moreover, the concept of the individual in the English school seems doubtful to him. It constructs its theory through personification of the concept of economic egoism. It sees both property and economic egoism as universal, but both of them are in fact historical and therefore relative. It follows that when a man with an abstract and one-sided element, not a historical man, takes economic action, the validity of the theoretical thesis must be strictly limited (pp. 353f.).

It is essential that 'economic phenomena are not limited to natural lawful representation of the real world, but appear only when human activity is added' (p. 356). Thus a national economic law never remains an expression of natural lawful effects in the real world. Knies states that once the 'historical method' was proposed, our specific tasks should be as follows:

> The factors in economic phenomena originating in the spiritual life of man teach us (1) that we encounter in the research of economic phenomena a correlation between the economic field and all other cultural fields, (2) that these factors are able to show a thread that binds the systems of politics, ethics and economics. And these factors are the cause of the continuous development observed in the economic life of peoples. It is this development that distinguishes the spiritual life of man from all other creatures. Therefore, the investigation of the economic development in people's lives becomes the task specific

> to political economy. It should first identify the historical figure of the national economy that moves stage by stage, and then discern the fundamental cause of this movement. As such, the theory of national economy is asked to explain the developmental law of the national economy.
>
> (Knies 1883:361)

Knies examines the stage theories of economic development put forward by Karl Heinrich Rau, Friedrich List, Roscher, and others (pp. 362–82). He finds in them descriptions of each stage, but they grasp neither their relation with non-economic spheres nor the correlation between the movement of all mankind and the economies of individual peoples especially. Roscher divided national economies into young, mature, and old periods, but nothing came out of this. He also presented a scheme of three periods, in each of which nature, labor, and capital were the main elements of production. According to Roscher, every national economy would follow this same circular pass, but Knies denies it, saying that this law could not be proved historically. Concerning Roscher's theory of circular stages, Knies was indeed critical, but he adopted the viewpoint of 'difference and similarity' from Roscher (p. 389) and stressed analogy. Analogy requires an important logical standing in order to understand Knies's conception of the political economy. What is his conception?

First, in natural science it is postulated that the same cause produces the same phenomenon, a conception that is also of great significance to real processes. But in a national economy, which has the task of surveying historical phenomena, one cannot expect that the same phenomenon will really recur, because spiritual-personal factors as causes of economic phenomena do not have the constant character observed in material things. However, there are constant factors in all human life and activity. Through them individuals are connected to the common whole, i.e. they belong to mankind. These factors also appear in community life (*Gemeinschaftsleben,* i.e., socio-politically ordered life), and so they are to be discerned in the economic activity of man. Moreover, the personal life of man develops continuously. As an individual follows this development from birth until death, so the organic whole of community life moves and develops. Changes may be seen only in terms of centuries. The sphere of economic phenomena cannot be cut off from the people's total life, so one can say that the economic sphere too is interwoven in the development of people's lives. If one is to discern the laws in economic facts, recognition of such laws must lead to the problem: what is the law of development? This law does not presuppose a constant that assigns a certain state, but that a state alters.

Next, the constant factors in life do not disturb the various expressions of men's personal lives with their own character in the variety of inner and

outer spheres. That is to say, such differences in the economic activities of people become visible. This variety can be recognized when developments of peoples reach the same stage in the developing course of mankind on the one hand (in the case of diachronic similarity), and when simultaneous appearance of similar phenomena in peoples (synchronic similarity) is at stake on the other.

If we are to compare the conditions and processes of national economies in various countries and periods, we have to deal with a law in due course, the law of phenomena that considers both similarity and difference. In this case we obtain only a law of analogy, not a universal law of causality. We must give up looking for such a law of phenomena in the economic sphere. It is important to show clearly the analogy that emerges lawfully in national economic phenomena. We should adopt a method that allows us to gain an insight into such an analogy (p. 479).

Analogous phenomena are defined as those that show coincidence up to a certain point, but beyond it present differences from each other. This coincidence gives substantial proof that both phenomena belong to the same genus. The difference is described as a consequence of their own specific conditions. Analogy can be seen not only in an individual phenomenon but in a series of subsequent phenomena as well, so that an analogy of development can also be recognized. The observation must reach to the phenomena and back towards their causes. Every fact can be grasped in its nature only when it is seen in relation to its cause. We cannot, of course, deduce analogy and its lawfulness from an individual causality. Co-incidence and difference can be grasped and proved only through comparison. Hence, we should identify individual facts in historical life correctly; then we can make use of these as the basis for recognition and reasoning. On the other hand, we can use a comparative method on a more comprehensive basis to understand individual problems, presenting as many analogous facts as possible. Therefore the historical study of people's lives—from antiquity to the modern age—is indispensable.

The study of analogy helps us to recognize the lawful in recurrent economic phenomena; it is also a way to reform the insufficient formulation of known laws. By increasing the number of related facts through a comparative survey, we may alter former lines of distinction and even progress to a new recognition of a wider genus:

> National economy must strive in principle to compare the continuously widening sphere of facts, and furthermore be ready to find more correct formulas about known lawfulness in phenomena on the one hand, and new laws on the other as a result of an increase of comparable objectives.
>
> (Knies 1883:481)

As seen here, 'lawfulness' in Knies's usage can be read as 'regularity'.

To widen objects continuously in this way and to conceptualize the results of observation by comparison may be a general style in scientific procedure. But we must remember that Knies proposed this approach in his criticism of the general validity of economic theory. It means that this approach admits the regularity found in parts of objects and defines the realm of regularity based on individual cases, and so it does not amount to a total negation of theory. Knies's attitude towards economic theory is characterized by this lukewarm feature. He planned this approach as concept-formation especially concerning economic phenomena. Here we can acknowledge some parallel with Weber's typology of economic sociology.

When we see the peculiarity of the German Historical School in its emphasis on the historical relativity of knowledge, the negation of a universal system, and the inclination to treat things as historical products and to oppose naturalism according to which society is treated as nature, here rises the danger of denying theory and of falling into unlimited relativism. To acknowledge the effectiveness of theory, some device is required to relate theory and history. Weber's ideal-typical formation of the concept was a response to this necessity and developed a new field of interpretive sociology *(verstehende Soziologie)*. Knies, who did not deny the effectiveness of theory as seen above, also proposed a law of analogy as a means to limit—so to speak—this effectiveness to a certain stage in the development of the organic whole of society. By doing so Knies, despite his strictly relativistic position, did not neglect theory. At the same time, he could unconsciously open the door to understanding history by means of an ideal-typical formation of concept, and to a perspective on economic sociology. Historicisation in German political economy led to economic sociology, to use Tribe's expression.

Knies's conceptional logic, which stresses historical development, follows the same line as Weber's sociology, which explains not development but change in terms of typology. It should be noted that the inclination towards sociology also seen in Schmoller (Tamura 1993: ch. 7; Schumpeter 1954:811–13) is already confirmed in the discourse presented by Knies. Knies showed the same kind of thinking in his concrete discussions as well. For example, in his discourse on money, he sufficiently explained, classified, and defined various functions of money without a direct appeal to analogy (Knies 1885: parts III–IV). We can see here how much his reasoning owed to the logic of analogy.

Knies claimed that Roscher did not fully understand 'the productive potential of the inductive procedure in the field of analogical facts and the necessity of uncompleted study to reach new truth' (1883:481). He viewed Roscher's cycle theory merely as settling known lawfulness, despite the fact that the future of the economic life of people is open. In this way Knies (1883:482) saw a profound truth in the words of Tommasso Campanella:

'analogy which leads us from known to unknown is the principle of all discovery'.[6]

Sitte

Knies's use of *Sitte* includes the double character of 'is' and 'ought'. This confuses his conception of economics and often draws criticism. First, to understand the background of his usage, we observe the complicated and changing meanings of *Sitte* in German intellectual history according to Ilting (1984).

Immanuel Kant sought a law of ethics *(Sittengesetz)* based on the validity of reason a priori, and here *Sitte* is conceived of as being reasonable and normative. In contrast, Georg Hegel, another great philosopher, presented a scheme in which *Sittlichkeit* would be realized at increasingly higher levels, i.e. from the family via civil society to the state. *Sittlichkeit* was almost identified with citizenship in a wider sense. Here we can discern a conception that *Sitte,* while having a reasonable and normative character, appears in the realm of community life. Following this approach, we encounter an appraisal which sees things that form and foster community life as *sittlich,* and things that damage and injure the community as *unsittlich*. In this context grows a specific view of history: higher *Sitte* is to treat the collective prior to the individual, and *Sitte* grows from a lower to a higher level as time goes on. In the nineteenth-century battlefield of nation-states, this view came to identify *Sitte* with culture as an expression of the spirit of the people *(Volksgeist)*. The reasonable normativeness stated by Kant totally disappears here, and the opposite—i.e. the traditional product in a historical process—is regarded as *Sitte*. By the middle of the century the meaning of *Sitte* changed from reasonable normativeness via the moral virtue of community life to tradition. The notion that the basis of a national community filled with historical individuality is to be *Sitte* has become a rather popular conception (Ilting 1984:891ff.). And Knies's use of this term could not be indifferent to this trend.

As a social scientist, Knies sought to understand *Sitte* at the level of existence (p. 140). On the other hand, he held a peculiar view of human development: individuals are integrated into mankind through people, and every man seeks to be a higher being. In this way Knies observes the development of mankind from the viewpoint of 'the development of man'. We can see in this notion a sort of optimism that Knies maintained about this development. Later in this discussion we will consider his use of *Sitte* keeping this framework in mind.

One of the important tasks of the German Historical School was to establish the teaching of political economy in order to contribute to the construction of Germany's national economy. For this purpose, the study of economic history as the history of national economic formation was

indispensable for List, the forerunner, Roscher, Knies, and others. They sought to oppose the absolutism of the English classical theory by means of a developmental law that would be induced from historical study. In the case of List, however, the task was to cope with the problems that originated because plural national economies at different developmental stages existed at the same time. That is why List was ready to accept the intellectual legacy of the Classical School for the future of Germany. But after him, the relationship between the 'developmental law' of history and economic theory was conceived in rather different ways. Generally speaking, the formation of a national economy meant the deepening and widening of the market economy, so that the analytic potential of the classical theory concerning the market economy was to be basically accepted even by economists of the Historical School. In spite of its inherent limits, opposition to theoretical absolutism was common to all of them, and so the difference among them is seen in the tactics of their opposition.

Making economics useful to national economic formation strengthened their attitude to consider economic policy as an integral part of political economy. The German tradition of cameralism and *Polizeiwissenschaft* may have sustained this inclination. This tradition was not in the least swept away by the introduction of Adam Smith, and with the contemporary institution of education and research, economic theory remained only in the small space assigned to it in the framework of jurisprudence, or *Staatswissenschaft* in the German academic world. To survey the history of formation of national economy by means of historical study was also regarded as an important function of political economy.

Classical theory, the partial validity of which Knies and others accepted as an analytic tool, had a view of progress and growth that presupposed the naturalistic assumption that uniformity and continuity spread from individuals to mankind. In contrast, the Historical School stressed with good reason the significance of the nation that they acknowledged from historical study, and could not relinquish the significant status of the nation between individuals and mankind. Classical theory could integrate history (the formation of a national economy), theory, and policy by means of the *homo oeconomicus* model and talk about the future from the progressivist viewpoint in economic terms. Knies, who denied the universality of this classical model, faced the task of presenting another image of humanity by which he could unite each sphere of political economy into a whole. He responded to this task by inserting *Sitte* and giving it the two-sided character of 'is' and 'ought'. And so the mode of concrete existence discovered by historical study always included the potential moment that would move to a higher existential level. In this way, development appeared as the development of a nation and of a national economy. One would be able to see the future as a result of national development. Knies indeed referred, from observation on the existential level, to the case in which various laws

and institutions changed *Sitte* as well as the case in which the change in *Sitte* led to the formation of new institutions. However, he did posit a view of economic development by introducing *Sitte* as if it were an independent variable, which moved the character of 'ought' from a lower to a higher level. He concluded that political economy is a science of man and that its proper objective is to explain the development of a national economy in terms of the development of man.[7]

For the Classical School, which depended on the substantial base of the early formation of the market economy and the deepening market in England, economic development as the progress of capital accumulation was already presupposed. And so when an economist examined, for example, the funds of capital accumulation in the theory of distribution, this procedure could automatically gain a status as the discussion of economic policy. In Germany, whose economic conditions differed greatly from England's, this theory could not be easily accepted as it was. Knies thought that the full blooming of self-interest and private property would damage community life. He hoped and even expected that *Sitte* would so develop that it would avoid this affliction and let the public spirit overcome self-interest. We can easily imagine why he eagerly took up such noneconomic elements as nationalities and religious consciousness in the concrete developmental process of history and mobilized elements of so-called historicism to give real ground to the prospective development. In doing so, Knies, who criticized the belief in a mono-linial stage theory of development such as in List, presented a logic that enables comparative consideration of various national characteristics—e.g. he proposed the study of analogy to show partial similarities in the patterns of economic development. This is why we can say that Knies made a step from historicism towards a typological sociology of the economy.

From the standpoint of classical theory, this view was seen as evasive in regard to economic theory. Specifically, the introduction of *Sitte* as an independent variable would theoretically deny the treatment of economic activity as independent and make it institutional framework dependent. Moreover, Knies saw there the dignity of personal freedom unbound by economic laws. And so critics like Schmoller and Weber would concentrate on this issue.

Schmoller criticized Knies for the denial of causality in personal factors and insisted that causality in social phenomena generally should be assumed (Tamura 1993:328–31). Weber (1975:191–4, 202) stated that increased freedom results in increased rationality, that free economic action therefore becomes predictable rational action and that this rational action, hand in hand with the pressure of market competition, fosters increased regularity.

Schmoller argued that as social scientists increase the objects of observation, they find causality in social phenomena. Knies, contented merely with establishing analogies, might appear to approach Schmoller's

position halfway. If one were to posit political economy as different from economic policy, regarded as merely an applied sphere, then the very law of development would be decisive. Acquiring a law of development through historical study would be the objective of political economy, and this procedure would be supported by the historical method. When the argument reaches this point, it must be divorced from Knies's intention. His relativism indeed limited the valid field of theory by mobilizing the approach of a sociology of knowledge, but he acknowledged—surely with certain ambiguity—the significance of theory in analyzing the market economy (Eisermann 1996:94–5). He would see Schmoller's viewpoint as substituting the law of development for economic theory by the historical method. Here he could have realized that his own position was different from Schmoller's. Because Schmoller was increasingly accepted by the academe, Knies may have sought to avoid having his title, 'from the standpoint of the historical method', understood in the meaning of Schmoller. He changed the subtitle in the second edition to reflect his methodological approach 'from the historical standpoint', leaving the text unchanged (Hütter 1928:76–7).

Historical background and perspective of the Historical School

The formation of the national economy in England increasingly advanced in the seventeenth and eighteenth centuries. To accelerate this process was the main challenge for developing countries, such as Germany and Japan in the nineteenth century. Whereas England's basic task was to foster capital accumulation smoothly, Germany's and Japan's was both to create the funds of capital accumulation and to integrate the national economy.[8] Moreover, it was not clearly conceived that this twofold task should presuppose the formation and deepening of the market economy. And the policy of catching up with England turned out to strengthen nationalism. This laid the groundwork for the idea that to distribute resources politically, the intervention of political power in the economic sphere was necessary, which in turn was affected by a great many non-market factors. Let us discuss the historical place of the German Historical School against the background of the general knowledge of economic history.

Protectionism and the theory of national productivity propagated by List were based on an early discernment of free trade imperialism that assured the interest of British industrial capital. Supported by the ideal of free trade *(Freihandel)*, Britain's overwhelming productivity discouraged the growth of industrial capital in less advanced countries, i.e. everywhere but in Britain. And the introduction of free trade *(Gewerbefreiheit)* amounted to excessive competition that led to the fall of traditional craftsmen and worsening social problems. To respond to these problems

caused by economic liberalism in the transitional period, Schmoller would propose a social policy for Germany. In proceeding this way, German theory became antipathetic to economic liberalism. In developing countries, where modernization and formation of capitalism were still to be realized, the consciousness of backwardness appeared as a repulsion of imported liberal economics. These historical conditions may have promoted a critical attitude towards theoretical absolutism, a historicist standpoint in political economy, a conception of economic development with historical stages, and so on.

But economists of the Historical School could not take part in socialism as critics of capitalism. Labor problems that became political issues in advanced Britain had already shown up in Germany *(Arbetterfrage)*. These economists accepted the situation as a crisis in the social order and regarded socialism as the factual and logical result of capitalism. They could therefore choose for themselves neither capitalism nor socialism. German historicism, born in response to the Enlightenment, inherited the legacy of the Enlightenment from the beginning and cherished a special concept of personality (Meinecke 1959: esp. ch. 9). Keeping their footing in this tradition, they rejected socialism as they understood it. They would take a position critical both of capitalism, which advanced the self-interest presupposed by the Classical School, and of socialism, which appeared as the denial of individual freedom and private property. Their position should appeal to the achievement of individual freedom and public spirit to overcome self-interest and to realize a just society. Its real base was to be found in the fact that man would develop universally towards the ethics common to mankind. Even Knies, however strongly emphasizing relativism, believed in universality. What brought about the development of man was *Sitte,* and its historical bearer was the people. Following this rationale, they had no historical and real presupposition other than the people *(Volk)* for the just society they were yearning for.

Here I have tried to apply a sort of sociological observation of knowledge to German political economy. Seeing it in this way, I cannot be content with an appreciation of the Historical School that depicts it as reactionary because of its opposition to economic theory. This can be said only if one regards the position of classical theory as right and progressive. In this connection, some spheres have always stood outside theory in human life, where goods and services—the definition of these is already problematic—are not always produced as commodities. Much more in the transitional period, where the way of needs and demands of individuals in general changed from so-called 'household' maintenance, with autarky and petit-commodity production, to that subjected mainly to the rentability principle and the maximization of utility, various problems appeared, not only economic, but sociostructual, ethical, and mental as well. In profit-seeking, for example, the idea of maximum profit conflicted with the idea of the

optimum. If one considers these problems in terms of a certain theory, that theory would surely have more utility than the self-satisfaction of an academician. But when a theory is to be considered absolute, how seriously can it treat the abuse of limited resources, the destruction of the ecological system, the production of 'public bads', public decision-making through plutocracy, one-dimensional valuation by mammonism, and so on? Such problems require solutions from the viewpoint of man.

Economists of the German Historical School were repulsed by the absolutism of theory because classical theory insisted that only its value premisses of man were 'right'.[9] They were willing to construct a future by means of such conceptions as *Sitte,* personality, and people, which later may have been regarded as conservative and reactionary. In reality, they would never try to go backwards in history.

Here I will try to interpret the ambiguity in Knies's vision. Whereas economists in the new Historical School discussed social policy in positive terms, Knies did not present such an attitude. This mystery would be solved by pursuing his personal history (Eisermann 1956:189–95). He could see no bearer of policy whom he could rely on. He hated and rejected the reaction to the March Revolution of 1848, moving to Switzerland, where he wrote and published *Politische Oekonomie.* German unification could not be achieved, and political liberalism had been defeated. At the time, economic liberalism was not identical with political liberalism. When the second edition was published, Germany had been unified by Prussia, but Knies was critical of its authoritarian character. It is true that he would be in a position to insist on the relativism of theory and on the intervention of economic policy against the evils of economic liberalism. However, he could not find any reliable bearer of economic policy.

We can perceive the same ambiguity in the abstract character of the concept of man that should incarnate Knies's *Sitte.* Surely he talked about the *Volk*. But that was not identical with the 'German Nation' unified in 1871; rather, it might be only the *Volk* of Knies's vision. Because of this ideal character, his image of man remained abstract indeed, lacking reality.

The link between Knies and Weber

Wilhelm Hennis seeks to examine connections that are historically and genetically relevant to Weber's work and that lead up to it. He sees these connections mainly in the German Historical School. When one traces the characteristics or specifics of Weber's science, he insists, one can easily see that his entire inaugural address is in accord with the traditional style of the Historical School (Hennis 1988:108, 127–8). In Hennis's view, a hint of that style is given by Knies, and so Hennis tried to follow the successive relationship from Knies to Weber. He says that Weber, after 'the new phase',

never departed from his own academic past, and concludes 'that Weber simply radicalizes the positions of the Historical School, including those of Knies' (Hennis 1988:142). Therefore, he has a very low opinion of Weber's article 'Roscher und Knies'. Let us use this work to examine the distance between Knies and Weber.

Knies contrasted the free and thus irrational-concrete action of a person, on the one hand, with the nomological determination of the naturally given conditions for action, on the other (Weber 1975:96). But Weber considers the free action of the individual as rational in the sense that its motive is comprehensible and thus susceptible to a meaningful interpretation of human conduct that is principally favorable to calculability. The lower this susceptibility becomes, the more free will tends to be denied, and so the relationship between the freedom of action and the irrationality of the historical event are in inverse proportion. In the case of a psychopathologic patient deprived of his own will, incalculability increases. According to Weber (1975:125–8), purposeful human action is highly susceptible to rational interpretation, and this fact allows the formulation of a generalization. Knies's process of analogy, in contrast, was content with acquiring similarity through comparative observation. In his view, irrationality originating in human freedom takes part in economic phenomena. And so to give a base on which regularity and generalization are to be acquired, he must widen the scope of observation.

The difference between these two positions is distinctive. Weber converted the conventional conception of humanity in the German Historical School. Hennis holds that the relationship between Knies and Weber, based on such a distinctive conception of humanity, is continuous, saying: 'All of Weber's special sociologies, led by the sociology of religion, are anticipated *in nuce* by Knies. Above all, Weber's theoretical orientation to action can be traced directly back to Knies' (1988:130).

Weber (1975:199f.) criticizes Knies's concept of personality. For Weber, the essence of personality is the inwardly consequent attitude towards ultimate value (Ohbayashi 1993:105). If one applies this view of personality to the bearer of science, the difference between the two becomes much clearer. Weber has this to say about the Historical School:

> With the awakening of the historical sense, a combination of ethical evolutionism and historical relativism became the predominant attitude in our science. This attitude sought to deprive ethical norms of their formal character and through the incorporation of the totality of cultural values into the 'ethical' *(sittlichen)* sphere tried to give a substantive content to ethical norms. It was hoped thereby to raise economics to the status of an 'ethical science' with empirical foundations.
>
> (Weber 1949:52)

Knies maintained his optimism for the development of man, believing in moral *(sittlich)* evolution to a higher level. This attitude allowed political economy to lead him from recognition of 'is' to that of 'ought'. The task of completing this reasoning academically was performed by Schmoller. The citation above is, therefore, typical of the critics of the Historical School from the standpoint of Weber, who considered it impossible to deduce 'ought' from 'is'.

Moreover, Weber argues at the end of 'Roscher und Knies' that Knies's concepts both of personality and of *Volk* are the application of organic theory, and charges that these are applied to the real ground of phenomena. This procedure of Weber might appear 'not at first clear' to Hennis,[10] but it was necessary for Weber, who was instrumental in transforming the conception of science:

> It is not the 'actual' interconnections of 'things' but the conceptual interconnections of problems which define the scope of the various sciences. A new 'science' emerges where new problems are pursued by new methods and truths are thereby discovered which open up significant new points of view.
>
> (Weber 1949:68)

When inhabitants of the 'iron cage' (formal-rational arena) dare to seek human dignity, they would have to expose their ideals to a sober value-analysis. It is indeed significant to reconfirm the universality of such traditionally recognized values as truth, goodness, and so on. But these highly abstract postulates of values as such cannot be used to judge the concrete means of politics. In the same way, social scientists whose object is a society composed of human beings cannot help but have an interest in what men become, what men are to be. But when a scientist seeks to justify certain political means as scientific, based on the results of the research produced from his own interest, he has to come into conflict with other interests. I have no objection to Hennis's (1988:197) opinion that neither personal needs nor interests but rather the strength and capacity for dedication define the real nobility of human beings. However, can a person be allowed to seek the legitimacy of his own value-ideal in the scientific validity of that value? Hennis stresses that political economy in nineteenth-century Germany is connected to 'that noble science of polities', and even Weber treated political economy as possessing a political character (1988: 108–9, 127). But because Knies incorporated the dual character of 'is' and 'ought' into *Sitte,* he allowed political economy to become automatically justified concerning its value-ideals by a process of gradual completion through successive periods. Is such a conception of science acceptable, when plural values conflict with each other and the realization of one value leads to the destruction of others?

Weber took this situation of his day seriously, and this is why he insisted on the 'objectivity of knowledge' and 'value-freedom'. His discussion proceeds from the acquisition of empirical knowledge to the right procedure for value-judgment. This is because he sought to make clear the limits of empirical science; he asked: What is expected when one holds onto the inwardly consequent attitude towards a certain value-ideal? This is a different position from that of the 'ethical economies' of Knies and Schmoller; it is also different from dedication to irrational decision-making.[11]

Hennis discerns in Weber's work an inquiry into the quality of man, and because of this he sees Weber as aligned with the German Historical School's tradition. But his conclusion is too abstract to identify the scientific character specific to Weber.

Notes

1 For a basic understanding of the German Historical School, see Schumpeter (1914:99–101). According to him, the historical standpoint, of which Roscher and Knies speak, involves historical-philosophical thinking, but Gustav von Schmoller's group lacks this perspective 'in the interest of unbiased historical *"Detailarbeit"*'. As a consequence, even Karl Heinrich Dietzel (1895:vi, 9), who was critical of the Historical School, admitted a complementary relationship of deduction and induction. And he would use the words 'Historiker' and 'socialtheoretische Forscher' in the same way. Here history became the positivist social science that would explain causally all human phenomena. From this point of view, Knies would be seen as an advocate of theoretical relativism.

2 In his 'Foreword to the Japanese Reader', Antoni suggested: 'History, the inexhaustible creator, always bears new, various and original works, activities and affairs, i.e., the individuals, whereas the structure of the human mind remains the same, universal and eternal. This formal uniformity is the precondition of historical cognition. Therefore the historism which seeks to historicize this *a priori* structure makes itself impossible' (1959:4).

3 See, e.g., Lifschitz (1914:149f., 168). On the contrary, Theodor Pütz (1936) appraised Knies as a forerunner of Friedrich von Gottl, the champion of the *Volk* conception.

4 Knies (1883:v–vii). This work is well known as unreadable; here and there Knies's logic appears contradictory. See Weber (1973:43; 1975:94–5).

5 On Roscher's 'historical method', see the foreword to Roscher (1843).

6 See Tamanoi (1978:188–91). Harrod (1971:26) stated that 'induction must be our primary tool for gaining knowledge about the world'. At the same time he admitted that almost all justifications of induction had not yet succeeded because scientists tried to absorb induction into deduction. Tamanoi refers to the affinity between Harrod's attempt to develop economics into social study and Knies's historical method (comparison and analogy).

7 Here I depend on the view of Deguchi (1968:51–8).

8 On the German unification, see Eisermann (1956:192).

9 For the problems that forced Harrod to be uneasy about economics, see Tamanoi (1978:189).

10 Hennis (1988:128). Among Weber's methodological discussions I cannot discern the difference between 'Roscher and Knies' and 'Objectivity', because he wrote

these in one series. While Hennis is very critical of 'Roscher and Knies', how does he evaluate the 'Objectivity' paper? I hold the conventional interpretation that sees Weber's methodological papers of 1903–6 as an entity.

11 Weber never discussed methodology without a purpose. This is readily apparent in his criticism of Lujo Brentano on *Arbeiterfrage* and in his discussion of the problem of productivity in the *Verein für Sozialpolitik*.

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Chapter 5

Lujo Brentano on the compulsory insurance system for workers in Germany

Sachio Kaku

That Lujo Brentano was a representative thinker of liberal social reform in the second German Empire (1871–1918) is well known. Born of an old Italian aristocratic family in Aschaffenburg, Bavaria, in 1844, he studied law and economics in Göttingen, then entered the Prussian Office of Statistics in Berlin. *Die Arbeitergilden der Gegenwart* (2 vols, 1871–2), the product of his study in England in 1868, established his position in the German academic world. Concurrent with the publication of this book, he served as a lecturer at the University of Berlin (1871) and as an associate professor at the University of Breslau (1872). In 1873 he played a role in the founding of the Verein für Sozialpolitik. As this activity shows, Lujo Brentano's career as a social scientist and a social reformer began in the early 1870s.[1]

Having published *Das Arbeitsverhältniss gemäss dem heutigen Recht* (1877), Brentano sought to determine the relationship between an economic order and a relief system and brought out *Die Arbeiterversicherung gemäss der heutigen Wirtschaftsordnung: Geschichtliche und ökonomische Studien* (1879) and *Der Arbeiterversicherungszwang: Seine Voraussetzungen und seine Folgen* (1881), intending to supplement his 1877 book. It is the aim of this chapter to characterize Brentano's views on Germany's insurance system for workers based on his books of 1879 and 1881.

An economic order and a relief system

The preface of *Arbeiterversicherung* begins with Brentano's recognition of the status quo: that the old order of trades was collapsing but a new one to take its place had not been firmly established.[2] The reason why governors failed in their attempts to initiate a new order of trades was, according to Brentano, that they tried to re-create the old conditions of subordination and obligation in a new form. He observed that the history of England shows that a new order of trades developed spontaneously, one that acknowledged the freedom of workers and reconciled it with the principle of the new order. 'It is possible', he wrote, 'to free workers from the

instability of their existence on the basis of the present economic order, through the realization of its basic principles' (1879:24). *Arbeiterversicherung* intends to prove this proposition.

Brentano enumerates the three basic theories of social democracy, by which he means socialism—the theory of the iron law of wages, the labor theory of value, and the theory of business cycles and relative surplus populations—and finds fault with the first two. The social democrats as well as the state socialists accepted Brentano's criticism of the iron law of wages, but they recommended a 'planned regulation of material production' (1879:15) in order to release workers who were exposed to more uncertainty than other classes. But Brentano questions whether such uncertainty is essential to the present economic order or whether it is a result of not having realized its principles and requirements concerning the employment relationship.

Workers and their families are exposed to two kinds of uncertainties: sickness, disability, and old age as well as an economic crisis. For workers who have no capital to cope with these uncertainties, reciprocity of support is the only measure that renders assistance in cases of distress. Therefore, the problem of how workers can eliminate the uncertainties that are created by an economic crisis or other reasons becomes a problem of how an insurance system for workers can be organized effectively. Brentano stresses that an insurance system for workers inevitably correlates with an economic order. By considering only this one point, he argues, all questions on the fundamental problems of insurance systems for workers can be answered.

In Book 1 Brentano gives a historical overview of relief systems, the first since Karl der Große, to demonstrate 'the correlation between self-responsibility and the ability to earn a living freely' and that between 'the ability to earn a living by special privileges and the constraint of foresight' (1879: 83).

The modern economic principles had been most clearly accepted in England; the propertied people were released from the obligation and responsibility to relieve the poor, the possibility and the obligation of self-help was given to the able-bodied, and welfare assistance was confined to disabled people. The repeal of the Statute of Artificers in 1814, the Combination Act of 1814, and the Poor Law of 1834 brought about the relief system that corresponded to the modern economic order. Since then, benevolent societies had increased in number, as well as various kinds of mutual aid associations, but employees were not obliged to join such organizations and employers were not obliged to make contributions on behalf of their employees. Thus, 'the foundation of the English aid association system rests on spontaneity and self-responsibility' (1879:70).

In Germany (Prussia) the Trade Regulation Act of 1845 [die Gewerbeordnung von 1845], the Decree of 9 February 1849 [die

Verordnung vom 9. Februar 1849], and the Relief Fund Act of 3 April 1854 [Gesetz, betreffend die gewerblichen Unterstützungskasse. Vom 3. April 1854] guaranteed the freedom to exercise any trade, and terms of employment were left to an agreement between employer and employee. The prohibition of combinations of workers was abolished. On the other hand, workers continued to have to make contributions to mutual aid association funds. Moreover, two laws of 1876 provided that workers were obliged to join a relief fund.

Dealing in commodity 'labor'

Book 2 examined the conditions that must be fulfilled in the case of commodity 'labor' under the present economic order, to lay the theoretical foundation of a social insurance system.

Employment is contracted freely just as one freely deals in a commodity generally, and nothing other than the terms of a contract restrict employers as well as employees, although 'labor' differs from other commodities insofar as it cannot be separated from the personality of its seller, the worker.

As other commodities, the production cost of 'labor' must be made up by its price, because it is impossible to sell a commodity under its production cost over a long period of time. Brentano believes that the following six conditions must be fulfilled in dealing with 'labor' under the present economic order:

1 The production cost of a commodity has to include the cost to produce not only each piece but also inferior pieces. In the same way, wages must be high enough for workers to support themselves when they are unable to work.
2 Producers of commodities are concerned not only that the price of a commodity covers its production cost, so they can continue to produce it, but also that the dead production cost arising from inferior items needs the least expenditure. Similarly, the second condition for a seller of 'labor' is to minimize the cost of living when he (the worker) is unable to work. The best way to achieve this is through insurance.
3 In this manner, the cost of labor consists not only of the cost of living and raising children but also of insurance contributions to support the cost of living when workers become sick, old, or unable to work, the cost of bringing up their children after the workers die, and the cost of burial. Thus, the third condition is to insure workers against six kinds of risk: i.e., bringing up children after their death, old age, burial, disablement, sickness, and unemployment.
4 To ensure that such insurance gives satisfactory results, contributions must be paid by relief funds without interruption, including when workers become sick or unemployed. The fourth condition, then, is to secure the economic foundation of the lives of workers.

5 If the right to relief were recognized only insofar as labor were bought by a certain buyer or in a certain market, the number of insurance contracts would be small and contributions would become high. Furthermore, this would make it difficult for workers to change employment, and the contributions that had been already paid would yield nothing in the case of a job change. Therefore, the fifth condition is that a relief fund cover all the workers in a trade throughout the country.
6 Considering the differences in the grades of risks in various trades, a relief fund should be founded in each trade or for workers who are exposed to similar risks. The amount of the contributions should also correspond to the extent of risk.

The relief system in Germany

In Germany, the Supplemental Law of Trade Regulation of 8 April 1876 [Gesetz, betreffend die Abänderung des Titels VIII der Gewerbeordnung, vom 8. April 1876] left it up to individual municipalities whether to require journeymen, helpers, and factory workers to join a health insurance plan. Brentano now explores how the health insurance system was working under this law. There were three types of system.

The first type of health insurance was a 'professional relief fund' that was founded by an order of municipal authorities. In 1874 in Prussia there were 1,642 relief funds for artisans of one craft with 146,982 members, and 1,161 funds for artisans of several crafts with 122,983 members. One fund averaged only about ninety-six members, an obviously insufficient number for it to work effectively as real insurance. It was also problematic that a local boundary was incompatible with demands of workers derived from the principle of freedom to live where they wished. According to Brentano, a local boundary of relief funds had one more disadvantage: the increase of old age necessitated raising contributions for all aged groups equally.

In requiring workers to join a relief fund, the law imposed on employers the obligation to register their employees in a fund, to help them to make contributions or to pay the full amount for their employees. But the present economic order did not recognize the right to work, and no relief funds provided unemployment insurance. Therefore, if workers became unemployed, they could not make contributions and so lost the right to relief.

Thus, a local boundary and the lack of unemployment insurance were the disadvantages of relief funds in Germany. 'In the case of these funds we cannot talk about in the exact meaning of insurance' (1879:142). For example, in 1876 in Berlin, 37.6 percent of workers were not insured in the case of sickness in spite of the obligation to join a relief fund and of the contributions that had already been paid.

The 1876 Supplemental Law of Trade Regulation provided that those who could prove that they had participated in another registered relief fund were exempt from joining a fund founded by order of a municipal authority. These registered relief funds included two types: 'company relief funds' established by the initiative of employers and so-called 'free funds' organized by those who joined neither 'professional relief funds' nor 'company relief funds'. Free funds consisted of funds founded by an association [Vereinskasse] and genuine free funds [eigentlich freie Kasse].

In Brentano's view, the company funds had various problems. First, most workers lost their membership in those funds with the annulment of their employment. Second, workers were forced to comply with terms that employers offered at dealing in commodity 'labor'. Furthermore, the right to relief could disappear with the bankruptcy of companies. Considering these problems, Brentano argued, 'obviously, in case of sickness, members of company funds can be much less insured than those of municipal compulsory funds' (1879:161).

The 'Hoffnung', a free health and burial fund founded in Breslau in 1877, was unable to cope with the requirements which were demanded for an insurance system from the viewpoint of the present economic order, because it raised contributions without regard to the age of members and excluded members who moved out of Breslau.

The definition of 'associational funds' was provided in the law, keeping in mind the funds of trade unions for their members. Hirsch-Duncker's Unions, which were founded as nationwide craft unions with local branches after the example in England, divided relief funds separately for sickness, disability, old age, and burial under the apprehension for insolvency; it also failed to provide relief for the unemployed. Brentano writes, 'Hirsch-Duncker's Unions do not give workers a chance to cover sufficiently the cost of labor by the price of labor' (1879:190).

In spite of the compulsory relief system, Brentano concludes, 'in Germany there is no relief fund for workers which affords them possibility to insure themselves in cases of sickness and for that reason implicitly also in cases of disability, old age, and death' (1879:190–1). Because existing relief funds did not enable workers to cover the cost of labor from wages, it might follow that public and private poor relief in various forms had to be provided for children after the death of their working parents, for unemployed, sick, old, and disabled workers, and for burying workers. However, this meant, according to Brentano, that the society had to bear a part of production costs, and thus these costs were a kind of subsidy for an industry in which those workers were employed. On the other hand, the relief was so scanty that privation and misery all too soon snatched away the lives of many workers. Furthermore, workers were embittered by the necessity of covering the cost of labor by mercy through poor relief, and driven to socialism. 'But, all these are incompatible with the basis and demands of

the present social, economic and national order' (1879:193). Individual self-responsibility was one of the principles of the present social, economic, and national order, which prohibited covering the cost of labor through poor relief. The equality of all people before the law was also one of the principles of the present order, a system that did not permit the state to subsidize employers as part of the production cost in the form of poor relief.

The insurance system and the role of trade unions

In the conclusion to *Arbeiterversicherung*, Brentano asserts that the following conditions are necessary for an insurance system for workers to be viable under the present economic order: (1) the provision of unemployment insurance, (2) a nationwide fund that has a wide base and enables workers to find the most favorable market, and (3) a correspondence between the amount of contributions and the degree of risk. Based on these conditions he formulates his idea of how an insurance system ought to function. First, the funds for bringing up children after the death of their working parents should be made available by life insurance companies through special life insurance; the same may be said of insurance against disability, old age, and death. Needless to say, the amount of admission fees and contributions must correspond to the degree of risk, and funds must be available to repay contributions that have been paid and accumulated.

Brentano prescribes a different treatment for insurance against sickness. This can be solved only by a mutual relief fund for each branch of trade. The same approach should be used for unemployment insurance. A fund for unemployment insurance must be well informed about conditions in the labor market, and only a trade union can be so. Thus, 'this insurance can be effectively undertaken only by a fund which is founded by fellow workers on the basis of reciprocity' (1879:207). So 'only a trade union can be a relief fund in the case of unemployment' (1879:210).

A trade union also plays an important role as a countermeasure against an economic crisis. Economic depressions cannot be eliminated in the present economic order, because they are inseparable from the individuality of consumption. But if, through the operation of a trade union, wages are high enough to also support workers during periods of unemployment, the destructive effects of an economic crisis are substantially removed, and 'workers have become economically independent, self-reliant, and confident in times of decline as well as in times of prosperity' (1879:220). Then, it is not only possible to solve the labor questions on the basis of the present social, economic, and national order. It is precisely the consistent implementation of the basic principles of the present economic order that leads to the resolution of these issues.

As Brentano understands the role of a trade union as stated above, radical reform of the Hirsch-Duncker's Unions would be out of the question. 'This

organization must develop out of the workers themselves and correspond to their needs and understandings; only then can it grow in harmony with the lives of workers' (1879:221–2). Since Brentano is doubtful about state interventions, he concludes that the only thing that should be asked of a state is that it should not disturb the development of a corporate organization of workers by its legislation.

The insurance system for workers in Germany: a supplement

In 1881 Brentano published *Arbeiterversicherungszwang* with the intention of supplementing *Arbeiterversicherung*. The goal of an insurance system for workers is, according to Brentano, to 'eradicate the dangerous socialist movement by resolving legitimate complaints of the working class' (1881: 16). The essential requirement to reach this goal is that an insurance system works effectively. Thus, the problem identified in *Arbeiterversicherungszwang* is to determine how an insurance system can be effective. After summarizing his idea in the former book *Arbeiterversicherung* in chapter 3, Brentano deals with workers' accident compensation insurance in chapter 4 and miners' funds in chapter 5.[3]

As long as the present economic order stands, Brentano tells us, an effective insurance system for workers cannot be realized by a compulsory insurance system, because income from which contributions must be paid is not guaranteed under it. But accident insurance is an exception to this proposition, for two reasons: first, 'the possibility of accidents threatens a worker only so long as his employment continues' (1881:36), and second, in the case of accident insurance, the economic consequence of accidents can be harmful not only to workers but also to employers. For these reasons, both of them are required to raise their contributions.

On the other hand, it is incompatible with the present economic order that the state pays a part of the contributions. Obviously this means that the state subsidizes part of the production cost of a commodity and that it makes a present to consumers at the expense of the whole. In Brentano's view, this is a monstrous injustice.

Miners and foundry workers obtained the same liberty to exercise a trade as other workers after the freedom of contract between employers and workers was recognized by the Law of 21 May 1860 and the prohibition of combinations was removed by the Trade Regulation of 1869 [Gewerbeordnung für den Norddeutschen Bund. Vom 21. Juni 1869]. But the legal requirement to join an insurance fund remained unchanged for them. In Prussia in 1879 there were eighty-four miners' funds, covering 2,146 mines, foundries, and saltworks. They granted their members sick benefits and burial money, relief in cases of disability, pensions for widows and orphans, and other assistance such as release from school fees. The

scope of their activities differed from fund to fund and between established and non-established members. As contributions were deducted from wages or offered as subsidies from employers, they were not paid and the right to benefits was lost if workers were laid off or dismissed. This reflected the contradiction that the freedom of trades was recognized on the one hand but the old compulsory insurance system still remained on the other.

In the case of the miners' fund in Saarbrücken, about 24 percent of the miners who paid the admission fee and contributions were not receiving sick pay and/or funeral benefits. This was also true of other miners' funds. Therefore, 'the results of this observation of the miners' funds successfully confirm my proposition that an economic order and an insurance system must be in accord for the insurance system to be effective' (1881:60).

Criticism and counterargument

In chapter 6 Brentano refutes the criticism that *Arbeiterversicherung* received and examines ideas that would make a compulsory insurance system effective. He rejects the assertion that existing relief funds were effective in their own way, offers evidence to refute the notion that temporariness of the insurance also has merit by reducing contributions, and criticizes the existing insurance system inasmuch as contributions mean, in fact, a concealed tax on the workers for the benefit of the poor. Furthermore, he points out that workers dislike the deduction from wages and that some of them leave funds because of it. 'A compulsory insurance system which provides no real insurance for workers who are obliged to enter it must drive them to social democracy [socialism] instead of separating them from it' (1881:66). The flat contributions by all members to cope with the absence of income, the respite of payment in the case of no income, or a combination of a relief fund and a saving fund—all of these ideas have a weakness in raising contributions. So, Brentano says, 'only a trade union can provide an insurance fund in the case of unemployment' (1881:74).

There were also plans to combine a compulsory insurance system and a trade union, but, according to Brentano, because 'only a very small fraction of German workers belong to the trade unions which are so far deficient in organization' (1881:77), the introduction of a compulsory insurance system would increase the power of employers over workers and prevent the formation of trade unions which would make the insurance system effective:

> A compulsory introduction of such associations of interested parties [i.e. trade unions] would contradict the duty of a state to treat all the members and all kinds of interested parties equally, just would be the case if the state prohibited trade unions or disrupted the conditions of their existence.
>
> (Brentano 1881:78)

> So long as the principles which are exhibited in the existing order of trade, i.e., the free agreement of working terms and the right not to work under the non-agreed terms, are valid, the compulsory insurance system cannot work effectively. On the contrary, this idea, if practicable altogether, would accord with the economic order which forces workers to take on any work at any price or at a price determined by the authority.
>
> (Brentano 1881:82)

Moreover, 'if one would not shrink also from the obligation of work, one would better turn to the plans of Adolph Wagner and Otto Arendt' (1881: 82). They developed the concept of compulsion elaborately and consistently: if their plans were realized, workers would be sure to receive relief in case of need, and contributions for the insurance would be raised through taxes. The nature of their plans is no longer an insurance system but a national poor relief system which borrows the name of insurance' (1881:83).

Brentano concludes that no change should be made in regard to his proof of the incompatibility of a compulsory insurance system with the current economic order which is based on freedom and legal equality, and of the correlation between the economic order and an insurance system.

In chapter 7 Brentano reflects on the types of jobs that guarantee workers so high an income that they can afford the contributions to insurance funds, once putting aside problems in regard to the economic order. He observes that such jobs fall into three categories. One of them is lifetime employment as a civil servant. If all employment consisted of state jobs, one need only base the effectiveness of the compulsory insurance system for workers on lifetime employment as a civil servant.

The second type is trade union jobs, because, in his view, trade unions lay the foundation for earning a living by privilege. Unions exclude workers outside of their trade and adapt the supply of labor to the demand. Through these measures they influence the terms under which their members will work and assure their income. Thus, members of trade unions are privileged:

> It was not unthinkable that in the course of time all workers would belong to one of the trade unions as in the age of guilds, and in this case all the questions of the effectiveness of a compulsory insurance system for workers would be solved. Otherwise, and if one would adhere to compulsory insurance for non-members of an association, only the compulsion to work under the conditions which would be decided by the authority would remain to make it effective. Where there are no powerful trade unions as in Germany, the introduction of compulsory insurance would have the effect of hindering the rise and expansion of trade unions.
>
> (Brentano 1881:89)

If the state compulsorily introduced an institution like an arbitration board and a corporation of workers as part of the arbitration system, such an institution would be subject to the state and state organizations, and the personal freedom of workers would be greatly restricted. Workers would no longer possess legal equality, even if a compulsory insurance system did become effective.

The third means to ensure the effectiveness of compulsory insurance is the compulsion to work. In this case, everybody must work under the terms determined by the state to receive relief in cases of illness, old age, or death, and the freedom of workers would be destroyed. According to Brentano, 'This would be a completely state-socialistic and purely bureaucratic solution of the question' (1881:92).

Thus, in these three cases, although income would be certainly secured, the state would resolutely influence the terms of employment and the conditions of the economic, religious, political, and social lives of workers.

The role of the state

In chapter 8 Brentano explores the role of the state in a nation's economy. If the economic interests of all individuals were closely connected with those of the state and the citizenry's positive feelings toward the state were enhanced, a sense of well-being and of cultural prosperity would perhaps be compatible with this social and political condition. However, 'if the moral, religious, and spiritual freedom of the individuals were suppressed, the source of all the great moral and spiritual progress would be choked and all further development of the national culture to greater, better and more ideal stages would be hindered' (1881:103).

From another point of view, Brentano is apprehensive about the mightiness of the state. To preserve the existing culture it is necessary that the lower classes benefit from its blessings, which at the time only the higher classes enjoyed. But to do so, the lower classes must be economically independent. He wrote:

> If it is characteristic of the new form of economic order to create the opposite of economic independence, it seems evident that it hinders rather than accomplishes the achievement of the goal of maintaining our culture.
>
> (Brentano 1881:104)

> If the economic, religious, political and social existence of workers depends only upon the state, and if it is the state that distributes the blessings of the culture among the various social classes, it is certain that the working class makes every effort to take possession of the

> state or to influence its control decisively. The same economic interest necessarily evokes the same endeavor among the other social classes.
> (Brentano 1881:108)

Thereupon the social classes antagonize one another, and 'the new economic organization that is now planned paves the way for achieving the goal of social democracy [socialism] instead of combating with it' (1881: 108). So Brentano warns against the mightiness of the state.

Characteristics of Brentano's view

In conclusion, let us consider what *Arbeiterversicherung* and *Arbeiterversicherungszwang* reveal about Brentano's views on the social insurance policy that was about to be established in Germany.

First, Brentano published these books to rebut social democracy [socialism] and to reinforce the legitimacy of the present order. In *Arbeiterversicherung* the problem is presented in opposition to the assertion of the social democracy that the worker organizations do not work well under the present economic order. *Arbeiterversicherungszwang* demonstrates how an insurance system can work effectively after confirming that its goal is to eradicate the social democratic movement. As we have also seen, the author examines various systems and proposals in terms of their implications for social democracy or socialism.

Second, what, then, is 'the present economic order' whose legitimacy Brentano would defend? In the preface of *Arbeiterversicherung* the principle of modern life is identified with 'freedom and legal equality' (1879:ix), and in the beginning of Book 2 it is explained in detail:

> The fundamental principles of all of modern public life are personal freedom and legal equality. In the irresistible victorious development these principles became important in all civilized countries and grasped the entire sphere of public life, also the sphere of economic order. In the sphere of economic order, these principles mean equal economic freedom for all and free self-responsibility for everybody.
> (Brentano 1879:90–1)

Thus, the modern society that Brentano endorses—i.e. the present economic order—is a society of freedom and equality, and in its economic sphere everybody is an independent buyer and seller of commodities. In the modern society everybody enjoys freedom and is responsible for himself. Brentano emphasizes that the freedom of self-responsibility and the ability to earn a living freely are correlative. In this way he values the freedom of individuals and takes precautions against the intervention of the state. This is reflected in the following statement:

> Such an order as hurts individualism at the root would be the greatest obstacle to the development of mankind.
>
> (Brentano 1879:218–19)

> Even if individuals' total dependence upon the state for their economic existence must raise the acting power of the state in the external sphere, and even if it would be compatible with economic prosperity and with a kind of cultural prosperity, the control which includes the entire moral, intellectual and social existence of individuals threatens to stifle their personalities.
>
> (Brentano 1881:101–2)

Third, the key to realizing the present economic order is, according to Brentano, that a market mechanism should work well for the commodity of 'labor' in the same way as for other commodities in general. He thinks not only 'that the labor question can be solved on the basis of the present social, economic and national order, but that just the consistent accomplishment of the basic principles of this economic order leads to the solution of the labor question' (1879:220–1).

Here the role of trade unions must become the object of consideration. As the example of England shows, trade unions place a seller of labor on a level with a seller of other commodities by adapting the supply of labor to the demand through voluntary supply control and the employment exchange service, and by relief in cases of unemployment. Brentano believes that a trade union must be nationwide to fulfill these functions.

Fourth, the present economic order has been realized through the historical development in European countries, England being at the head of them. Brentano also regarded Germany as a modern society, as he wrote: 'Trade regulation law which holds good today brought the freedom of trade in full measure for the whole German Empire. Everyone is entitled to carry out any business independently' (1879:78). But the present economic order in Germany remains unfinished. In reality, trade is restricted, and freedom and equality have not been accomplished. For instance, trade unions have not developed well in Germany. Hirsch-Duncker's Unions, which were based on the English model, did not offer unemployment insurance and divided various kinds of funds separately for fear of becoming insolvent:

> German trade unions do not perform one of the most essential tasks, perhaps the most essential one, and are able to be proud of only a few strikes, the value of which was doubtful and which resulted in unhappiness for ten years of their existence. Therefore they have been quite useless for German workers up to now. This is enough to account for their lack of progress, and even their retreat from the social democratic movement might well be left unsaid.
>
> (Brentano 1879:187)

With regard to the insurance system, it was problematic for Brentano that whereas the freedom of trade and the freedom of combination were recognized, joining a relief fund was obligatory. He considered these policies to be inconsistent.

Brentano also criticizes the German insurance system for workers *per se* for two reasons: (1) the limitation that insurance funds were founded in firms and/or municipalities, and (2) the lack of unemployment insurance. The insurance funds were too small in scale to work effectively, and contributions that workers had made would be nullified if they were discharged or voluntarily left their jobs.

Fifth, how does Brentano think that these problems can be solved? Unquestionably, Brentano regards historical development as important:

> Only the English arbitration boards work very well, because the employers and especially the workers have nearly one hundred years' experiences in labor disputes.
>
> (Brentano 1881:90)

> Why should our trade unions not divest themselves of defects? Why should our workers not awake from their current social democratic illusion and try to improve their condition by a means which is available under the present national, social and economic order? It should not be forgotten, however, that social and economic organizations can take root and work successfully only as a result of a historical development. It takes time for various relationships and for the people involved to mature.
>
> (Brentano 1879:223–4)

Brentano thus sets his hopes on the spontaneous development of trade unions, while he is critical of the state's intervention. On the other hand, he offers no concrete plans to solve the questions of the moment, although he describes an insurance system that he believes is ideal.[4]

And sixth, it is clear that Brentano's views are typical of those scholars who founded the Verein für Sozialpolitik in this respect: they held that the present economic order should be defended against socialism, although admittedly it has various problems, which are basically attributable to the labor question. On the other hand, however, we find Brentano unique among the members of the Verein für Sozialpolitik in his confidence in the function of markets and in his belief that Germany's economic problems can be solved by trade unions. This is shown by the fact that Brentano's two books received much criticism; indeed, *Arbeiterversicherung,* which Brentano dedicated to Schmoller, highlighted the difference between them.[5]

Notes

1 See Brentano's autobiography, Brentano (1931). J.J.Sheehan (1966) is a comprehensive study of Brentano and helps us to understand his idea and its development.
2 *Arbeiterversicherung* is composed of two parts that were originally issued as separate papers, namely, Brentano (1877, 1878).
3 Chapter 1 of *Arbeiterversicherungszwang* also emphasizes that contemporary problems can be handled scientifically. Chapter 2 sketches the method of economics, focusing on the relationship between observation of phenomena and deduction, and the correspondence of the propositions to the reality.
4 We have seen Brentano criticize the German insurance system harshly. As his criticism was too abstract and fundamental, Brentano and his critics argued at cross-purposes. Cf.Adickes (1879, 1881); Conrad (1880); and Miaskowski (1882). To make his criticism persuasive, Brentano should have been more in touch with the reality of the system—how far and how often workers moved in Germany at that time, how the insurance system really worked, and whether that system could ave been improved, albeit step by step, by various revisions.
5 Schmoller praised Brentano's article 'Erwerbsordnung und Unterstützungswesen' when it was published in 1877, but he censured Brentano's other article 'Die Arbeiter und die Produktionskrisen' in 1878 for the uncritical acceptance of the inference from Adam Smith and the doctrine of free trade. When Brentano wanted to dedicate *Arbeiterversicherung* to Schmoller, Schmoller thanked him for the sign of friendship but asked Brentano to indicate that there were differences of view between the two in many points. See Brentano (1931: 109–10). For the tension between Brentano and Schmoller in the late 1870s, see Sheehan (1966:79–84).

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Chapter 6

Anonymous history in Austrian economic thought

From Carl Menger and Anton Menger to Friedrich von Wieser

Kiichiro Yagi

Since Joseph Schumpeter's reflection of 1926, the *Methodenstreit* (debate on method) between Carl Menger and Gustav von Schmoller has usually been interpreted as an unnecessary conflict between two directions in economic research, theory, and history.[1] Using an architectural parable, Schumpeter assigned Menger an elegant salon in which Menger could luxuriate as a victorious theorist. At the same time Schumpeter praised Schmoller for the design of the grand house of which Menger's salon was just a part. However, this conciliatory interpretation misses an important aspect of the debate, because Menger's claim for methodological individualism—'exact orientation of theoretical research' (C.Menger, 1963:54; MGW 2:31) —was not confined to the status of an abstract theory in its static sense.

Organic genesis of institutions: another aspect of the *Methodenstreit*

In *Untersuchungen über die Methode der Socialwissenschaften, und der Politischen Oekonomie insbesondere* [Investigations on the Method of Social Science and Political Economy in Particular], Menger maintained that the 'exact orientation of theoretical research' that is grounded in the basic disposition of individuals—namely, action guided by self-interest—is also applicable to the emergence of various institutions. In human history, such institutions as law, money, village, state, and so on are the 'unintended results of historical development' (p. 130; 2:141). Such an 'organic origin' (p. 133; 2:145) is most properly interpreted as the synthetic outcome of the cumulated actions of selfish individuals; a holistic concept such as 'the nation' is not required to explain historical development. Though, of course, Menger admitted the intervention of the conscious action of a collective will or of the state in historical development, this 'organic' perspective was the core of his view of history.

Schmoller was rather indifferent to this aspect of the debate. Except for briefly commenting that 'it is not distinguished by surprising novelty'

(1884:985), he refrained from discussing it. Schmoller also rejected the charge of holism and stressed his empiricist position that favors statistics and historiography for the inquiry of collective phenomena. Thus, seen from a broader perspective of intellectual history, an alternate scene appeared in this debate in relation to the tradition of historicism in German academics. While the opponent of historicism, the methodological individualist Carl Menger, was deeply attracted by the idea of 'organic' origin that had been first emphasized by the founder of the Historical Law School, Carl von Savigny, the leader of the German Historical School in economics, Gustav von Schmoller, distanced himself from his precursor. He even sneered at his opponent's enthusiasm about the 'organic' view of historical development.

This twist comes from the difference between the basic attitude of the two Historical Schools towards existing social institutions. Whereas the economists of the German Historical School—particularly the later version—were interventionists who supported the protective tariff and social policies, jurists of the Historical Law School preferred the spontaneous growth of judicial institutions to artificial codification and pragmatic legislation. According to Menger, there are two types of the origin of institution: the 'organic' origin, which has no collective will, and the 'pragmatic' origin, which is guided by a collective will. Applying this dichotomy, we can say that whereas jurists favored the former, economists advocated the latter. The reason why Menger was so supportive of Savigny's position was not confined to his recognition of the significance of the question that Savigny raised: 'How can it be that institutions that serve the common welfare and are extremely significant for its development come into being without a common will directed toward establishing them?' (p. 146; 2:163).

Menger also agreed with Savigny's desire to protect organic development from the 'impetuous' rationalistic efforts of reformers who intended to eliminate the element that 'is not sufficiently understood' in order 'to create something new in the realm of political institutions' (p. 177; 2:207).

Menger applied Savigny's position to economics. It is clear that the *Kathedersozialisten* (socialists on academic chairs) around Schmoller were in Menger's mind when he warned against shallow pragmatism:

> The aim of the efforts under discussion here had to be, on the contrary, the full understanding of existing social institutions in general and of organically created institutions in particular, the retention of what had proved its worth against the one-sidedly rationalistic mania for innovation in the field of economy. The object was to prevent the dissolution of the organically developed economy by means of a partially superficial pragmatism, a pragmatism that contrary to the intention of its representatives inexorably leads to socialism.
>
> (C.Menger 1963:177; 2:208)

In Menger's view, the original contribution of historicism in the German-speaking academic world lay in its demand for 'full understanding' of the existing social institutions, especially the institutions that have developed 'organically'. Menger thought that this 'organic' genesis of institutions could be explained as 'the unplanned outcome of specifically individual effort of members of a society' (p. 155; 2:178) without recourse to collective holistic entity such as the 'Soul of the Nation'. Jurists or ethnologists of historicism counted language, religion, law, and the state as the social phenomena that come into being without the distinct will of particular persons. From the field of economic phenomena Menger added market, competition, money, traffic customs, division of labor, systems of trade, and business customs to this series of social phenomena with an 'organic' origin. Menger explained the generating process of money to be as follows:

> difficulty in barter → discovery of the good that is widely demanded → use of that good as a means of exchange by few persons → its diffusion by imitation of the success of others → formation of the 'custom' → emergence of money as the general means of exchange

Various kinds of goods have naturally different degrees in finding those who want them. Based on this fact, sooner or later some people will recognize the merit of using appropriate goods as the means of exchange. Even in the situation where they cannot exchange their goods for desired goods, the exchange of goods that are more widely demanded is a step forward, because they attain more favorable position to appeal to those who have the desired goods. Then, after observing the success of a person who entered the indirect exchange by utilizing some appropriate good as the means of exchange, many will follow him or her. As this becomes the prevailing 'practice' in the marketplace, the direct exchange becomes obsolete and useless. A special kind of good that is chosen by the spontaneous formation of this 'custom' finally attains the position of money: 'The economic interest of the economic individuals, therefore, with increased knowledge of their individual interests, without any agreement, without legislative compulsion, even without any consideration of public interests, leads them to turn over their wares for more marketable ones, even if they do not need the latter for their immediate needs' (p. 154; 2:176).

Once money appears in this way, additional elements such as the standard value of money, the supply of coins, and then the issuing of paper money that has legal validity within a territory, and so forth are integrated by the government. Menger neither overlooks nor opposes the intervention of the state in the formation of institutions at this stage:

> It is clear that legislative compulsion not infrequently encroaches upon this 'organic' developmental process and thus accelerates or modifies the results. The unintended genesis of social phenomena may factually be the exclusively decisive social development for the first beginnings of social formation. In the course of social development the purposeful encroachment of public powers on social conditions becomes more and more evident. Along with the 'organically' created institutions there go those which are the result of purposeful social action. Institutions which came about organically find their continuation and reorganization by means of the purposeful activity of public powers applied to social aims. The present-day system of money and markets, present-day law, the modern state, etc., offer just as many examples of institutions which are presented to us as the result of the combined effectiveness of individually and socially teleological powers, or, in other words, of 'organic' and 'positive' factors.
>
> (C.Menger 1963:157–8; 2:181)

In an advanced society, various social institutions are the product of the collective will or of purposeful legislation. Menger did not deny the appropriateness of the 'pragmatic orientation' that explains the essence and origin of these institutions from the aims and available measures for those who created them. But it is worthwhile to note that he did not confine the effect of the 'organic' factor in the operation of socioeconomic institutions to past stages of human development. Menger avoided the non-interventionist failure of the Historical Law School, but according to him the basic tenet of legislation should be that it does not deny the individual interests that have hitherto supported the 'organic' development of institutions: 'The fruit of their view was not to be the avoidance in principle of positive law development, however well stipulated. It had to be the purification of the latter by new insight gained from the thoughtful consideration of common law' (p. 234; 2:286).

Carl Menger versus Anton Menger: organic origin and power relations

Menger's attack on Schmoller failed to provoke a definite and detailed response. In my view, it was another Menger, Carl's brother Anton, who offered the desired answer concerning the meaning of the 'organic' origin of institutions as well as the necessity of 'pragmatic' legislation for social reform. To a jurist of the two or three generations after Savigny, the Historical Law School's 'wisdom' that social institutions are embedded in spontaneously emerged custom was obsolete. In the introductory part of his *Das bürgerliche Recht und die besitzlosen Nationalklassen* [Civil Law and the Non-possessing Class] (1889), Anton wrote: 'The basis of our

juridical institutions, in particular those of private law, was founded by custom far before the beginning of our historical knowledge. Since the basic frame of the juridical organization existed when states and legislation emerged in the historical development of the society, the task was only to enrich it by adding detailed regulations' (A.Menger 1908:5). Anton's interpretation of this process clearly contradicts that of Savigny:

> Since the basis of our modern legal order stems from custom, the natural outcome is the formation of a legal system that favors the interests of the selected few before those of the mass.
>
> (A.Menger 1908:5)

> All the private legal institutions of the modern age are not the product of the whole nation, but that of the privileged class. They were imposed on non-possessing classes by the privileged through struggle over a thousand years.
>
> (A.Menger 1908:9)

Grounded in this view, his criticism of the preceding juridical schools is strikingly radical:

> If it is the reality that four-fifths or nine-tenths of the whole nation are deprived of almost all of the comfortable interest for a lifetime by the regulations of the private law, who can believe the saying that these regulations are created by the soul of the nation? It is also a contradiction that through an explicit or implicit contract consent is given to them by which the majority of the nation are assigned the unfavorable position stated above.
>
> (A.Menger 1908:9)

Anton did not deny the historical development of institutions. We can construct the logical steps of such development in his case, too. What corresponds to Carl's reflections on the difference in the marketability of goods is the difference in the physical or other sorts of power that individuals possess. The results of this difference are the power relations in society that intensify over time. The judicial order is no more than the reflex as well as the means of the existing 'social power relations'. Therefore, in Anton's case we observe these steps:

> struggle for interests in primitive conditions → the dominance of the mightier → development of social power relations → emergence of the mentality that considers the existing relations as normal → formation of the legal order that protects the established privileges

A legal order generally has a conservative tendency. This tendency is all the more strengthened by the translation of the law of custom into the

written law. On the other hand, the power relations in society change in accordance with social and economic development. There appears thus a tension between the conservative legal order and the changed power relations in society. For this reason, Anton maintained, the 'jurisprudence for legislative policy' should have a broad social perspective in order to reconstruct the legal order that corresponds to the emerging power relations. In his inaugural lecture on assuming the presidency of the University of Vienna in 1895, Anton made a passionate appeal for this requirement:

> Every juridical order is a grand organization of the power relations that has grown out of the historical development within a nation. When the interest of the ruling class is claimed continuously, it transforms laws and regulations so that they are approved as the given objective order by the rest of the nation. However, once the power relations stated above have changed definitely, laws and regulations are deprived of their natural grounds. The state of the struggle for interest will reappear in the society. It is the mission of Social Law Science to observe the change in the power relations in their depth so as to be able to recommend future reforms of the law.
>
> (A.Menger 1895:45–6)

Concerning the impact of modern economic development, Anton counts the emergence of large cities and large industries and the formation of the working class as the salient changes in 'social power relations'. To these he adds political changes such as the introduction of general education, universal suffrage, and mandatory military service:

> Most of the principles of the present civil law have their origin in the age of absolute monarchs when most people were very poorly educated and the protection of social peace was assigned to trade companies. In the modern age, when universal suffrage and secular education, and mandatory military service in particular are introduced in most parts of civilized nations, such a kind of civil law is not sustainable without great reform.... In the age of the Roman Empire most of the laboring people were in the situation of slaves. No regulation existed for them, since the Roman law treated slaves simply as goods. Various juridical devices had to develop to mitigate that harsh treatment even during the mediaeval and the following ages. Further, in the modern age when the working class has emerged generally as a mighty national class, making a new great system of legislation for this class has become an urgent task for us.
>
> (A.Menger 1895:47)

The contrast between the Menger brothers' views of history raises two questions. First, is Carl's 'exact orientation of theoretical research' applicable

to Anton's 'social power relations'? And second, if their basic views of historical development are incompatible, which view is incorrect?[2]

As far as value and price theory is concerned, two views seem to be incompatible at a first glance. As Carl argued in Book One of *Untersuchungen*, the influence of power on economic action is excluded together with that of 'non-economic motives' as well as 'errors'. He called this exclusion 'the dogma of complete freedom from external compulsion' (p. 85; 2:75) and regarded it as the necessary condition for construction of theory. All present-day economists recognize that essentially the same assumptions have generated an everlasting controversy since then.

A closer look reveals that Menger's price theory is not completely deterministic with respect to its concept of the price struggle. Within the range determined by economic conditions, a tougher or luckier negotiator will obtain a larger gain from the transaction than one who is weaker or not as lucky. But this is probably not what Anton had in mind when he used the term 'power relations'. In the case of Carl's price struggle, both partners can be better off and the difference will become negligible when the result is considered on the social level. If we should seek the manifest element of the 'power relations' in this area, which is now referred to as *microeconomics*, it is the initial condition that the productive factors (capital, labor, and land) are unequally distributed and owned by different social classes.

The situation is different in the application of the 'exact orientation of theoretical research' to the diachronic development of social institutions. As we explained about the diffusion of the indirect exchange by recourse to the observation/imitation of the action of others and to the formation of practices/customs, the 'exact' explanation of the 'organic' process contains certain social elements together with the influences of 'errors' and 'uncertainty'. Carl mentioned market, competition, traffic customs, division of labor, business customs and so forth as economic institutions of an 'organic' origin. But all of them have to intersect other series of 'organically' developing institutions: 'power relations' and the state. The core issue here is the emergence of property. Though the institution of private property seems to occupy the central position in the view of the 'organic' origin of social institutions, it is difficult to explain its origin merely by exchange. Carl could account for the origin of money convincingly by the gradual increase in the advantage of the indirect exchange. But contrary to the exchange relationship in which both partners can improve their well-being, the institution of private property improves only the well-being of possessors and deprives others of any possibility to use the goods concerned. Therefore, it is hard to assume the emergence of the institutions of property from the natural extension of the selfish actions on both sides.

In Carl's *Grundsätze der Volkswirtschaftslehre* [Principles of Economics] of 1871, the institution of property is discussed in the second chapter,

'Economy and Economic Goods'. Note that this belongs to the elementary part of his theoretical system which comes much earlier than the chapters on commodities and money. Carl maintains that the conscious economic action of an individual begins with the recognition that the quantities of goods available are smaller than the quantities required to fulfill his or her needs completely. The goods concerned become 'economic goods' that should be used efficiently and for whose acquisition human efforts (production and exchange) are directed. Under this quantitative relationship of the comparative scarcity of resources (goods) to needs, the following situation emerges:

> If the quantitative relationship under discussion occurs in a society (that is, if the requirements of a society for a good are larger than its available quantity), it is impossible, in accordance with what was said earlier, for the respective needs of all individuals composing the society to be completely satisfied. On the contrary, nothing is more certain than that the needs of some members of this society will be satisfied either not at all or, at any rate, only in an incomplete fashion. Here human self-interest finds an incentive to make itself felt, and where the available quantity does not suffice for all, every individual will attempt to secure his own requirements as completely as possible to the exclusion of others.
>
> (C.Menger 1950:96–7; MGW 1:55)

In this situation of scarcity, the salient features are inequality and collision of interests, both of which can easily induce violent conflict. In Carl's view, the necessity of the institution of property is given in this unstable situation:

> In this struggle, the various individuals will attain very different degrees of success. But whatever the manner in which goods subject to this quantitative relationship are divided, the requirements of some members of the society will not be met at all, or will be met only incompletely. These persons will therefore have interests opposed to those of the present possessors with respect to each portion of the available quantity of goods. But with this opposition of interest, it becomes necessary for society to protect the various individuals in the possession of goods subject to this relationship against all possible acts of force. In this way, then, we arrive at the economic origin of our legal order, and especially of the so-called protection of ownership, the basis of property.
>
> (C.Menger 1950:97; 1:56)

In *Grundsätze* Carl spoke of only the necessity of the institutions of property in relation to the possible disorder of society; he did not deal with the

process that leads to the foundation of the legal order. I do not think that he would not oppose the 'organic' origin of this core institution of society. But the 'organic' process that leads to the foundation of property might differ considerably from that of the origin of money. Whereas in the latter case an institution that is beneficial to everyone emerges through the actions of self-interested individuals of equal rank, the former is grounded in inequality and conflict of interest. This 'organic' process does not necessarily exclude Anton's view that the mightier justified their factual dominance by juridical institutions. If we use the parable of a game, exchange is the game through which every participant can be better off, whereas the struggle for the possession of goods is a zero-sum game.

Indeed, in appendix VIII to *Untersuchungen*, Carl tried to understand the 'organic' genesis of law in light of his 'exact orientation':

> The same external situation in which family heads of a territory find themselves under the most primitive conditions plus the insecurity, common to all, of the products of their individual efforts, cause the oppression felt most keenly by all others, too. It is human nature to feel the continued threat of evils almost more acutely than the threatened evils themselves. Each individual, even if not directly harmed, feels that his interests are most seriously threatened by acts of violence, especially the weak individual, who is always in the majority compared to the strong one.
>
> (C.Menger 1963:225; 2:274)

Carl also finds here the progressive steps toward insight regarding individual interest and its diffusion among the people. First, the wisest few who 'can recognize their permanent interest beyond the shortsighted interest of the moment' realize the necessity of imposing a limit to unfettered selfish acts. Gradually this insight occurs in the minds of all who have a potential advantage in that limit to end violent conflicts. 'Among these are even the strong individuals, whose interest requires the conservation of what their power has achieved' (p. 225; 2:274). Then, still gradually, this becomes the consolidated conviction of a nation.[3]

If the mutual recognition of the possession emerges despite the unequal distribution of ownership, it is owing to the progressive insight of individuals that the benefits of legal stability are more important than the possible gain by the seizure of goods in another person's hands. Although the mutual recognition of the possession does not increase the individuals' present goods, the development of the economic activity (production and exchange) will improve their future economic situation. This kind of recognition of individual interest at a higher level might cover approval of the privilege of the mightier by the weaker for the sake of survival, or 'voluntary subjection of the weaker to the protection of the stronger' (p. 157; 2:179).

If such approval is to be found behind the rights of the rich and mighty, Carl's 'exact' interpretation of 'organic' origin does not contradict Anton's view of the 'power relations' in society. Despite the basic difference in the structure of the primitive situation, it is the approval of individuals from the viewpoint of their long-term interests that promotes the development of the institution.

If such approval is unlikely to be expected, then we have to adopt Anton's view that the present legal order was forcefully imposed by the mightier to conserve the existing power relations. In appendix VIII, Carl admitted another way to the genesis of law, that by force and authority. At first he called the order imposed by power 'statute' *(Gesetz)* in place of 'law' *(Recht)* that has an 'organic' origin. However, he anticipated the amalgamation of the two in the later historical development (p. 229; 2: 280). It suggests that the two are not always discernible in many cases. Thus we can conclude that Carl had to make a concession to Anton.

Friedrich Wieser on power and mass politics

Despite all his ambiguity and concessions, Carl Menger adhered to methodological individualism throughout his life. As he also remained an old-type liberal who was reluctant to allow the state to intervene in the private sector, he could be counted as a 'substantial individualist'.[4] It was his disciple and the successor to his chair at the University of Vienna, Friedrich von Wieser, who dared to introduce a new view of the individual and society into Austrian economic thought. He further tried to establish an updated liberalism based on a redefinition of freedom.

Wieser started his academic career by producing two books on Austrian value theory in the 1880s. While a professor at the German University in Prague (1884–1902), he witnessed the turmoil caused by the Badeni's language decree of 1897. With the rise of Czech nationalism, the Charles University, then the oldest in the Habsburg Empire, had been divided into Czech and German institutions just before Wieser's arrival. During the turbulent days of the 'language struggle' the two Charles Universities inevitably became centers of the turmoil. Although the requirement that public officials know both languages meant, from the viewpoint of Czech students, that equality had finally been attained, to the Germans it represented a merciless deprivation of any hope to enter public administration.

In a lecture he presented as president of the German University, Wieser interpreted the essence of the 'language struggle' as the appearance of the new 'mass' in the political process:

> Our Austria is now in the midst of the political confusion and many think such an immaturity in politics has been never witnessed hitherto.

> However, we should not forget the following: Though the appearance of the great masses who have not been politically trained so far has necessarily brought about a fierce turbulence, it is still in itself progress in political education.
>
> (Wieser 1901:347)

When the 'mass' becomes the center of politics, the liberal political theory that advocates 'the rule by the contract of individuals' loses its reality. Mass politics reveals the aspect of the domination of the state:

> The essence of the state is domination, and the domination is not borne by the contract. Those who wish to dominate call for a struggle, because the struggle stirs the instinct in the depth of the life of the mass. The secret of the life of the state lies in the secret of the life of the mass. To understand the state, we need first to understand the psychology of the individuals in the mass and, further, to know the general technique of the manipulation of the mass.
>
> (Wieser 1901:349)

A convinced liberal, however, Wieser would not accept the use of power in mass politics as it was. According to him, primitive power is merely an external force that can dominate people with the threat of physical force (external power). To become a complete power that can establish right and order among people, the mass must be equipped with the internal power that forces the approval of others. The following remark on Austrian politics in 1905 flows directly to the reflections in *Recht und Macht* [Right and Power] (1910), which investigated this theme theoretically:

> Through their national awakening Czechs could not immediately recover their political rights, but formed merely a new political power. How this power transforms itself to the right depends on the way and the strength with which Czechs exert the power on one hand as well as on the way and the strength with which all other groups exert their power.
>
> (Wieser 1905:56)

Another basis for Wieser's reconsideration of liberalism was the labor movement, which was encouraged by the idea of socialism. After his return to Vienna, the working class influenced by socialism (the *proletariat*) became the main focus when Wieser talked about the 'mass' in politics. In reality, those socialists who wished to mobilize the working classes for the class struggle were pioneers who recognized the significance of the 'mass' and 'power' in modern politics. In October 1905 they succeeded in organizing the mass demonstration for universal suffrage that filled Vienna's main streets with workers shouting political slogans. The composition of Wieser's *Recht und Macht* revealed its impact; it began

with an examination of Ferdinand Lassalle's idea that the real power relationship is the true constitution;[5] then, after providing a criticism of the materialist conception of history in Marx and Engels's *Communist Manifesto*, it presented a revised version of liberalism. As he sought the coexistence of two nations in Bohemia, it became Wieser's next task to teach the Austrian middle class the possibility of coexistence with the advancing working class.

Wieser's first reflection on labor problems can be traced to his article 'Grossbetrieb und Produktivgenossenschaften' [Large Business and Productive Cooperation] (1892). Grounded in an analysis of the inevitable development of the hierarchical structure in large-scale production, Wieser pointed out the survival of the functions of entrepreneurs and administrative clerks in the productive cooperation that was originally conceived as the alternative to the capitalist form of the private firm. Wieser justified the search for an alternative form of production in that there was a contradiction in the capitalist form of production in its treatment of workers as a subordinated labor force though it provided them with the experience and consciousness of a 'mass'. But alternative forms such as productive cooperation also cannot establish a sufficient productive base insofar as they adhere to pure democratic principles that exclude entrepreneurs and clerks. Therefore, the growth of alternative forms of production advances only in accordance with the progress of stratification within the working classes, which in turn proceeds hand in hand with their cultural maturity.

Before World War I, Wieser thus did not share the anxiety of the middle class that the victory of the working classes might bring a return to barbarism.[6] In his later words, 'The majority that is only barbaric is not enough to establish an eternal victory. Breaking the law of oligarchy is realized only on the condition that the majority affords the inner value of appreciating the merits of the minorities' (Wieser 1910:90). As long as the present middle classes retained their productive functions, they would also find their positions under socialism.

As Warren Samuels (1983) suggests, Wieser's view of management was close to that of Schumpeter in regarding entrepreneurs as 'leaders' in economic life. For Schumpeter, however, the 'mass' had only a negligible significance compared with the heroic leader, 'entrepreneur'. In contrast, Wieser focused on the state of the 'mass' in which 'power' and 'leadership' were conceived. Even in the transitory period when workers were unable to control production, they nevertheless created an organ for the struggle. As Wieser later put it, the 'organ of the mass' countervailed the 'leading organ' of the capitalist firm:

> The Lassallean idea, 'let soldiers vote their officers', is realized within the organized proletariat in the form of the election of the leaders for

> the class struggle. This is a step to freedom, or to 'power' … But the legions of workers have so far not succeeded in influencing work discipline within the firm, not to say management. Entrepreneurs ardently defend their authority to impose work discipline and regard any intervention as a declaration of war. They reject it with all of their power as if it were an encroachment of private property.
>
> (Wieser 1910:123)

Does this struggle lead to a social revolution, as Karl Marx taught? Here, Wieser turns his eyes outside the capitalist firm. In the entire society, even workers who form an impressive 'mass' within the capitalist industries are not necessarily the majority of the people. The organizational form of the large business may be a serious problem to the industrial proletariat, but not to other social classes such as farmers and shopkeepers. The same is true for the bourgeoisie that dominate large firms. They are only a part of the ruling block. Another part of the ruling block, the conservative group, has even supported social legislation that the industrial capitalists have opposed. According to Wieser, this lack of monolithic domination is the guarantee of freedom. The struggle among classes promotes the stratification within each class and thus may open the future space of freedom:

> In economics it is the law that the self-interest of individuals turns out to be for the benefit of the whole by way of free competition in which everyone behaves as an egoist toward each other. Similarly [in politics], the dominant [class] egoism might be redirected to serve the whole by the resistance of the countervailing egoism based on collective solidarity. After a fierce struggle the top of the proletariat may attain the position of social power along with present power groups. But at that stage, as once on the side of bourgeoisie the unified liberal party had to separate, division will emerge inevitably within the now monolithic proletariat. Its sign is seen already among the proletarian leaders who apparently established their power within the state. The law of stratification is also valid in the case of the fourth rank.
>
> (Wieser 1910:127)

Wieser maintained that a 'redefinition of freedom' is necessary to revive liberalism in an age of organized economy and mass politics. According to him, the classic liberalism has two basic errors in its view of man. The first is the supposition that everyone has the same strength. Refusal of the 'protection of the weaker' based on this supposition discredited liberalism. 'Another probably graver error is that it treats man as a free being, although he is never so in reality' (p. 133). In Wieser's view, man lives in a world where various social powers interfere with each other and thus is influenced by those powers both internally and externally. He might be bound

unconsciously by an 'ethical power' that penetrates the depths of the mind. Or he might be obsessed by certain thoughts and knowledge, or be forced to act according to social standards of status and possession, of the group or organization. Further, he might be subject to the order of the legal or political authority. These are all social powers that influence the real person. The first error of classical liberalism also stems from ignoring the effect of social powers. The difference in the strength of individuals is not totally attributable to individual traits but to the forms and constellation of social powers around them.

The 'redefinition of freedom' thus cannot be an individualistic one that does not recognize the constraints on human behavior, but a social one that prescribes a certain state of the constellation of social powers. It means a state where no power is so strong that it exerts an overwhelming effect on individuals, but where the coexistence of multiple powers is sustained in a balanced order so that individuals perceive no coercion from the outside. In other words, it is a state where a stable order is sustained by the powers that influence man from inside, that is, by the powers that individuals use voluntarily under the balancing equilibrium of external powers.

It was the emergence of various forms of social powers, such as labor unions and cartels, that Wieser envisioned when he formulated his new concept of freedom. These are the spontaneous products of the efforts of both workers and entrepreneurs to achieve their interests. The growth and struggles of 'wild powers' that recognize only their own interests and limited solidarity consciousness may undermine the state of freedom. Wieser here assigned the role of government as intervention. Freedom is maintained only by active intervention of the government under the principle of the 'public welfare' that regulates the relations of social powers and keeps the balance. Wieser thus justified interventionism under the name of liberalism.

Concluding remarks: social elements in anonymous history

After consideration of Wieser's reflection on 'social powers' and his effort to revise the meaning of liberalism to permit state intervention in a mass society, the question naturally arises: How does this sociological reflection relate to his economic theory? There are two opposing answers to this question. The one that is submitted by Streissler (1986) is simply that Wieser was so muddle-headed that he did not take the discrepancy seriously. The second, that of Ekelund (1970) and Ekelund and Thornton (1987), maintains that Wieser's theory is a precious contribution that provides a bridge from neoclassical utility theory to social economics. In my view, the latter is more convincing, though it has some weakness in

its too hasty reduction of Wieser's power theory to the individualistic interpretation.

Ekelund and Thornton (1987) warn against misinterpreting Wieser's concept of the 'mass' as a collective entity. 'Consider his use of the terms 'leadership' and the 'masses' —terms which might seem indicative of a collective interpretation of society or history. Actually Wieser appears to have meant only 'innovator' or 'entrepreneur' by the term 'leader' and 'competitive imitators' by the term 'masses" (p. 105). Although I agree with their warning against holism, I cannot overlook the peculiar problem setting when Wieser talks about the 'mass'. Remember that Wieser stressed the 'psychology of individuals in the mass' in his reflection on the 'language struggle'. Further, he replaced the notion of the 'free man' with a balanced state of social powers. Then, we can assume that the 'mass' is a psychological state of individuals in which they are highly sensitive to the influence of the social powers. We need not regard the 'mass' of the working class as a collective entity, but we need to recognize the strong tendency of individuals who are counted in that 'mass' to respond to the stimulus in similar directions. Contrary to this state of the 'mass', we can conceive of the psychological state that excludes the influence of social powers. This is the state of the 'idealized' economic man with which economic theory starts. Indeed, the real state of man is not always that of the 'mass', but at any rate a social state where individuals are not immune from social influences.

But does this answer just shift the difficulty to the concept of 'power'? It raises another question: Are 'social powers' collective entities? In his review of Wieser's *Das Gesetz der Macht* [Law of the Power], Otto Hinze (1926) interpreted this concept as the substantiated motives of individual action that Max Weber developed in his sociological theory. This is an attractive suggestion that enables us to translate Wieser's sometimes unclear description into the language of the methodological individualist. But we must admit that there also exists an appropriate level of analysis that considers the interaction between individuals and 'social powers'. If these 'powers' take some definite shape—as customs, sentiments, norms, role structure, legislation—they may be called institutions. Individuals seek their interests not freely but under the influence and the constraints of institutions. Their cumulative actions promote the emergence and alteration of institutions that are sometimes represented by definite actions of the leaders.[7]

In the memorial lecture of the hundred years' anniversary of his *alma mater,* Wieser revealed that he had been fascinated by the idea of writing the 'history of the anonymous masses' [*namenlose Geschichte*] since his youth (Wieser 1907:339). In his youth the models were Leo Tolstoy's *War and Peace*[8] and Herbert Spencer's *Introduction to Sociology*. But his efforts can be interpreted as the resumption of his teacher Carl Menger's reflection

on the 'organic' development of institutions. In Menger's case it was Savigny's romanticism that stimulated his reflection. In contrast, Wieser's models are marked by a wider perspective that contains the dynamics of the power and the mass. The experience and observations of the 'language struggle' and class struggle gave him rich materials to transfer Menger's reflection to politics and sociology. Wieser thus became the Austrian counterpart of the social economist when Max Weber planned his grand series of *Grundriß der Sozialökonomik* [Outlines of Social Economics]. It is understandable that the influence of this view of 'anonymous history' can be traced in the works of later Austrian masters like Ludwig von Mises, Joseph Schumpeter, and Friedrich von Hayek.

Notes

1 See Schumpeter (1926). For the background of the *Methodenstreit* and its impact on the later generation of the German Historical School (particularly on Max Weber), see Yagi (1997). The present discussion relates to its Austrian counterpart.
2 Eugen Ehrlich was one of the Viennese students who was torn between the two Mengers. The outcome of his agony was his sociology of law. See Ehrlich (1913).
3 It is, however, difficult to glorify the mere equilibrium of the horror in the zerosum game with the graceful adjective 'organic'. To be the 'organic' genesis of a law, an additional element is necessary. Carl seems to be forced to admit the growth of such a non-individualistic concept as 'the idea of close solidarity' or 'the awareness of national community' (C.Menger 1963:227; 2:277) though in a modest form of the accompanying phenomena.
4 The distinction between 'methodological individualism' and 'substantial' or 'political individualism' was given first by Schumpeter (1908). In Yagi (1989) I discussed Menger's pessimism in his later life in relation to his reflections on the rationality of individuals.
5 Note that Lassalle was the source of ideas on which Anton Menger built his criticism of the existing legal order and his concept of social law science. See Kästner (1974:10, 54, 63).
6 Streissler (1986) pointed out that Wieser admired fascists (Wieser even wrote sympathetically about Hitler's failed coup attempt) in his *Gesetz der Macht* (1926). He also called Wieser a 'racist' and an 'admirer of authoritarianism', referred to his 'unclear mind', and so on. My interpretation is based mainly on his writings before the war, though I do not deny the consistency of the core idea of 'power' between prewar writings and postwar writings.
7 Concerning this level, Ekelund and Thornton (1987) propose the view of the emergence and alteration of institutions by the selfish actions of individuals that sounds like a new institutionalise explanation of the development of institutions. But as an old institutionalist W.C.Mitchell also praised Wieser's *Theorie der gesellschaftlichen Wirtschaft* (1914) in the preface to its English translation (Wieser 1927), the line between both directions in the institutional economics is very fluid.
8 Tolstoy's view of history in *War and Peace* was nicely described by Isaiah Berlin (1953).

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Chapter 7

Gustav von Schmoller and Werner Sombart

A contrast in the historico-ethical method and social policy

Shin'ichi Tamura

With the increased interest in the German Historical School in recent years, it is becoming clear that Werner Sombart, as a representative of the youngest Historical School, played a decisive role when new problems in German social science were identified at the turn of the century.[1] Sombart was critical of Gustav von Schmoller's social policy and methodology and attempted to ride over him.

In his 1897 essay 'Ideale des Sozialpolitik', Sombart attacked the perspective of ethical economists who viewed the ideal of the social policy not from economic life itself but heteronomously based on disciplines like ethics and religion. According to him, 'instinctive anxiety in regard to big capitalist development and a preference for all forms of the small economy —peasants, craftsmen, small domestic industrialists, etc. —characterize ethical economics and Christian economies' (Sombart 1897:33–4). The latter was a particular attack on Schmoller.

According to Sombart, Schmoller was a reactionary who attempted to protect the old middle class and to restrain capitalistic development. Sombart presented this criticism systematically in the first edition of *Der moderne Kapitalismus* in 1902. Schmoller, however, felt that Sombart had misunderstood him. In the opinion of Schmoller, Sombart interpreted the demand for ethics only as the outdated 'moral of the aunt' and overlooked the fact that social regulations as a whole are problematic (Schmoller 1903: 299). For Schmoller, 'ethical' did not mean interference with economic development. However, in the second edition of *Der moderne Kapitalismus* Sombart came to partly accept Schmoller's view. It is the aim of this chapter to discuss which part of Schmoller's view Sombart eventually accepted, and which he continually criticized and why.

Schmoller's ethics and social policy

Schmoller often emphasizes the ethical superiority of agriculture and small business over big business. For example:

> Agriculture is driven by the free air of nature, not by the profit in town life. The craftsman knows the customer for whom he works…. Their relationship has an ethical character…. Today, domestic industry has even greater merit…namely, the combination of industrial labor, agricultural, self-sustaining economy, and the family life of husband, wife, and child.
>
> (Schmoller 1908, 1:466, 473, 490)

Based on these statements, Sombart's criticism seems reasonable. However, Schmoller was not trying to sustain the traditional, bucolic economic life, but, on the contrary, attempted to promote modern industrial society politically.[2]

Protection of small business and social policy

In his 1870 publication, *Zur Geschichte der deutschen Kleingewerbe im 19. Jahrhundert,* Schmoller explains his insistence on ethical social policy. Therefore, it is no exaggeration to say that this book holds the key to an understanding of that policy. In it Schmoller answers the following questions: first, what caused the distress of the crafts in the 1860s that was accompanied by a surplus of craftsmen? And second, is it still possible for craftsmen to be independent?

With regard to the first question, Schmoller states that the cause of the distress is an easygoing tendency of craftsmen to get independence prompted by the introduction of business freedom. He quotes interesting facts from petitions that were presented to the German Board of Trade in various localities; e.g. 'The small cities are, in many cases, inhabited by craftsmen who are poor, badly trained, immature, and poorly equipped with tools, and whose number exceeds demand. . . . [These men] are rushing into businesses that do not need funds' (1870:96, 115).

In the petitions Schmoller finds small businessmen who refuse to adapt to the modern industrialization process. They do not want to become factory laborers; moreover, they have neither the money nor the ability to found their own company. They behave simply to become independent just on the impulse of the moment. These petitions reveal 'a truth that is often overlooked by the enthusiasts for economic freedom': 'The more deeply man descends in the economic classes, the more his behavior is regulated, not by the recognition to be in the best position economically, but by a nearsighted desire for enjoyment and a momentary tendency toward inactivity. That is, immoral secondary motives of various kinds constitute the psychological factors that the economist must consider here' (1870: 117). This is, for Schmoller, the existing counterevidence to 'the rational economic man' in liberal economics.

As for potential independence in the crafts, Schmoller thinks that, especially in the processing industries for finished consumer goods which

the factory system had not yet entered, it might be possible for craftsmen to be self-sustaining and to expand their businesses, because of the slow pace of technical innovation and the importance of hand skills. He describes the dynamic activities of the able master who could call himself the owner of a factory. This individual rose by developing new goods, introducing machines, and achieving specialization after the traditional crafts dissolved (1870: 198–9). Moreover, Schmoller draws attention to industrial development in England and France through symbiosis with the expansion of the putting-out system and the small business (1870:571ff.).

According to Schmoller, although there is an objective possibility that the crafts can develop as middle and big businesses, many craftsmen lose that opportunity because they lack economic rationality, market knowledge, technical ability, and so on. In the conclusion of this book, Schmoller praises the ablest master with the words 'self-made man'; he could become the owner of a big factory—whereas he criticizes the small master of a large majority of crafts who is used to sticking to the traditional manner and rule and depends on inherited property (1870:666–8). Moreover, such traditional small businesses constitute the main export industry in Germany by means of cheap labor, such as the Silesian textile industry. Here, the profit-making greed of export industrialists was keeping the traditional form and cheap labor of the crafts.

By protecting small business, therefore, Schmoller aims to reform the consciousness of traditional craftsmen from within, i.e. by teaching 'economic morality, such as a diligence, effort and saving', and 'imbuing [them] with a spirit of business enterprise' (1870:679, 325). Through such social policies, he attempts to promote the development of traditional craftsmen in modern industrial society and to give them the chance of 'participating in classy culturally advanced goods, education, and welfare' (1904:55). Schmoller believes, then, that with ethical policies 'the difficult social problem would not exist' despite inequality of income (1870:672), in contrast to the *laissez-faire* society which causes class struggles between the bourgeois and the proletarian through the accumulation of unearned income.[3] But he assumes that economic morality derives from diligence and the savings of the traditional household economy before modern industrial society (1870:181–2). The misinterpretation of Schmoller occurred from this reason. The ethical social policy of the state was, for Schmoller, the means to raise a rational economic behavior from the old economic morality, not to maintain the traditional norm and behavior.

Mercantilism

Schmoller used the results of empirical research to prepare for the construction of a new system in the national economy. According to him, the economic phenomenon could be explained by two different causal

relationships, 'natural and technical causes' and 'psychological and ethical causes' (1904:57). The old economics, which is based on the hypothesis of the selfish economic man, considers only the phenomenon brought about by natural and technical causes. On the other hand, his ethical economics is based on psychological and ethical causes. It means understanding an economic phenomenon as the operable cultural one.

Schmoller attempted to integrate these two causal relationships by means of Wilhelm Dilthey's psychology (1883:979). He explains that each human being who has a naturally instinctive desire and impulse gradually acquires an ethical public feeling, and this feeling as a centripetal force forms various organizations of the national economy. This public feeling is, therefore, the existing cause of a unification of the national economy (1893:13). While it crystallizes in the progress of history into a feeling of justice in the national economy, it creates political, legal, and economic institutions and organisms, such as the family, the community, and the state (1900–4, 1:61) Under Herbert Spencer's influence, Schmoller interpreted economic progress as a process in which such institutions and organisms differentiated in a complex manner and then were reintegrated. This process signifies ethical progress in which the public feeling develops from the natural impulse.

Schmoller applied this concept to his stage theory and notion of mercantilism. According to him, economic development reached by the extension of an exchange economy to the national boundary cannot be explained without the influence of politics on economy.

> Political organisms and economic organisms are by no means necessarily conterminous; and yet the great and brilliant achievements of history, both political and economic, are wont to be accomplished at times when economic organization has rested on the same foundations as political power and order.... In its innermost kernel [mercantilism] is nothing but state making—not state making in a narrow sense, but state making and national-economy making at the same time.... The essence of the system lies...in the total transformation of society and its organization, as well as of the state and its institutions, in the replacing of a local and territorial economic policy by that of the national state.
>
> (Schmoller 1884:3, 37; 1896:3, 50–1)

Schmoller understands mercantilism as a revolutionary policy with which the modern nation-state dissolved the old social and economic structure and promoted the modern national economy.

Historical development of the business enterprise

Later, Schmoller attempted to place the small business in the historical development of business enterprise. He calls the crafts 'a small business that

is linked with the household economy of the owner' and that is 'the origin and germ of the full industrial business enterprise at a later stage' (1900–4, 1:419). In his understanding, 'generally a group [consisting] of the merchant, the owner of the putting-out system, and the industrialist emerged from them [craftsmen] for centuries' (1908, 1:466).

Schmoller considered the business enterprise from two viewpoints: from its nature of human-technical organization and from its relationship with the market (1900–4, 1:413–14). Entrepreneurship was the unification of the directing ability to manage rationally and the trading ability to assume a risk and pursue a profit. Schmoller believed that the mental traits of an entrepreneur were the product not merely of capital or the profit-making impulse, but of the ethical, legal, moral, and social limitation of unrestrained greed.

He thus divided the formation of the putting-out system into two types: the merchant controlling the small producer who is isolated from the market, and the producer himself having both a trading activity and the opportunity to extend his business. While the former makes the small producer a proletarian, the latter raises him to an entrepreneur. According to Schmoller, the small producer's self-sustaining agricultural production is the basis of his resistance to the unlimited exploitation of the merchant (1900–4, 1:426). Moreover, this resistance has not only a passive meaning, but also an aggressive meaning for the development of business enterprise. For example, the crafts guild guaranteed that craftsmen who have begun an activity for market from the early days became 'the technical master' (1908, 1:466). Schmoller evaluates the competition regulating association, such as guild, trade union, cartel, as an organization which defends the able producer from excessive competition and unfair business. Of course, these organizations—because of their egoism—promote a monopolistic policy that is often beyond the regulation of competition. Schmoller assigned to the government the duty of providing for controlling of unfair business practices.

Corresponding to this historical research, he theoretically divides all incomes into unearned income and earned income. For Schmoller, the regulation of competition means that earned income corresponds to the present contribution of small farmers, craftsmen, and entrepreneurs (1900–4, 2:425). It depends on a realization of the just market price of the goods they supply. Schmoller's concept of just price should not be identified with the one advanced in the Middle Ages. He holds that the people will judge a market price to be just, not when the price is fixed by the power and the thoughtless use of economic superiority, but when it is considered to be a cost-corresponding and reasonable price, which will probably change with a change in the standard of living and technical innovations (1900–4, 2: 115–16). Schmoller's concept of just price seems, in this sense, to be synonymous with the natural price in classical economics.

When Schmoller states that any limitation of the principle of equality except equality based upon human traits and achievements is arbitrary (1881:25) and then he requires the redistribution of income from the viewpoint of justice in the national economy, it is in his mind to guarantee the earned income to producers at the just market price on the one hand, and to impose a tax on part of the unearned income that the unfair business bears on the other. It means restraining the domination of the bourgeoisie and giving the craftsmen the chance to rise by self-help to the status of the small and big entrepreneur. Schmoller defines capitalism as a *laissez-faire* system dominated by the unlimited profit-making impulse (1903:298). For him, capitalism was nothing more than a system that suppresses the spirit of business enterprise and hinders the development of a fair market society.

Sombart's attack on Schmoller

The younger members of the Historical School, who had a sense of crisis in both domestic and international politics in the face of rapid industrialization in Germany in the last decade of the nineteenth century and the imperialist policy of the world powers, must have considered Schmoller's protectionism for small business rather tame. From their viewpoint, the ethical social policy of the Prussian bureaucrat sought by Schmoller must be transposed by social policy for capitalistic development, as Max Weber observed on behalf of the younger generation (Weber 1904:159).

The first edition of Der moderne Kapitalismus

In the first edition of *Der moderne Kapitalismus* Sombart intended above all to end the completely useless discussion about the progress of industrial development in the last few years, which was represented by Schmoller, and to construct a new system of social policy (Sombart 1902, 1:xii, xxxii). His most important tactic lay in removing psychological ethics from the causal explanation of economic development. For this purpose, using the anti-ethical system of Karl Marx characterized by extreme objectivism (Sombart 1894:551, 559), Sombart tried to deal critically with the Historical School by finding comprehensive explanations drawn from the very origin, i.e. the motives of living human beings that produce economic development (1902, 1: p. xxix). In other words, the economic principle that prescribes economic life in one age with characteristic peculiarity appears as a compound of mutually interacting motives of the economic subject (1902, 1:4).

Sombart conceptualizes the production of crafts as an extremely human business activity. It is an expression of personality that aims to satisfy a desire to reach a suitable social standing in life [Nahrungsprinzip] and to

achieve independence with 'empirical skill (1902, 1:79ff.). In contrast, capitalism provides an economy with which to pursue an abstract objective purpose that can be quantitatively grasped, i.e. profit-making. The economic purpose is separated from the individual personality of the economic subject and is considered only from the impersonal viewpoint of raising capital value (1:196). Sombart's concept of the crafts is much more romantic than that of Schmoller, who defined them as the half-business enterprise. Also, Sombart's concept of business enterprise is regarded as more impersonal than Schmoller's.

Moreover, according to Sombart, capitalism came into existence outside the crafts economy in a peculiar historical situation in the late Middle Ages with the rapid spread of a monetary economy. He depicted the development of capitalism as a process that caused the crafts to disband. The traditional economic morality and economic rationality that had been unified under Schmoller were now sharply separated and confronted as Nahrungsprinzip vs. kapitalistischer Geist.

As for the process of economic development, Sombart, in contrast to Schmoller, refused any positive role of the state from the viewpoint of theoretical thinking. In early capitalism [Frühkapitalismus] the natural development of capitalism was disturbed for various reasons (1902, 1: 409ff.). Among them were expenditures for unproductive purposes of the accumulated property, especially war, and a drastic reduction in population caused by famine, the plague, and war. State funds were spent to promote the economic policy in mercantilism, maintain a standing army, and procure public loans. All these activities continually exhausted any accumulated capital.

War and colonial expansion always absorb the productive power of labor and act to paralyze capitalistic energy. Sombart held that such factors prevented the growth of small business into big business. On the other hand, he emphasized that, in contrast to the stagnation of early capitalism, one could see the rapid growth of high capitalism [Hochkapitalismus]. In this, the formation of the big city as a consumption center increased the living standards of the middle class, and technological advances all played a decisive role.

For Sombart, the expansion of capitalism to agriculture destroys the latter's self-sustaining economy and produces a surplus population. This surplus population migrates to the big city which offers the possibility of high wages owing to the accumulation of industrial and commercial functions, and finds individual emancipation from the constraints of a rural community (1902, 2:235, 237–8). Sombart pictures the rich masses emerging with the growth of the middle class and a service-oriented economy in the big cities as people enjoy consumption and leisure in music halls, sports clubs, or restaurants, or pursue their fascination with horse racing (1902, 2:268). His vision of capitalism is the appearance of a mass consumption

society and is different from that of Marx, who predicted the collapse of capitalism.

On such a theoretical plane, Sombart attempts, finally, to confront Schmoller's argument regarding small business. According to Sombart, Schmoller and his generation made the competition between big and small business the problem: for them, to win through competition meant the realization of the economic reason for cultural improvements. From Sombart's viewpoint, however, winning through competition meant having the adaptable ability to organize production rationally and flexibly in response to the changes in demand. What seemed to Schmoller to be competition between big and small business is really nothing but competition between two economic forms: the crafts and capitalistic business enterprise (Sombart 1902, 2:430).

The economic field that Sombart discusses here is the one in which capitalistic small businesses come into conflict with the crafts, such as the building industry in the big cities. He states that if a craftsman had such an ability to adapt, he would be a small capitalistic entrepreneur already. Thus, the small capitalistic entrepreneur rises from among the craftsmen with a trading ability not because the protective policy is successful, but because there has been a selection and an adaptation in capitalistic competition (1902, 2:465).

Sombart, therefore, concludes that the reason why a craft is not promptly ruined is because hindrances to competition exist. It is, however, an illusion that with a producer's cooperative association it remains possible for the crafts to compete, and as well as that a legislative loophole allows the exploitation of apprentices (1902, 2:544, 566ff.). In other words, what Sombart wanted to prove finally is that the crafts, which should have been ruined, continue to exist because of artificial hindrances to competition. He recommends that labor laws for big business be applied also to the crafts and that job training for young laborers be required in addition to the education of apprentices for further capitalistic development (2:579–80).

Based on this conclusion, the difference between Sombart's and Schmoller's views on the actual recognition of the crafts seems not to have been so great. It was merely, as Schmoller himself pointed out, a difference between optimism and pessimism (Verhandlungen 1897:132), i.e. Schmoller intended to bring up the craftsmen who have a trading ability, whereas Sombart advocated such a protective policy only to keep the old crafts. But Schmoller did not believe that it was possible to maintain the old crafts just as they were. An important difference in both outlooks was their vision of capitalism in the future. Whereas Schmoller insisted on an ethicization of capitalism to form an affluent society in which a class struggle could be mediated, Sombart held that progress in high capitalism itself creates an affluent mass consumption society. However, Sombart also argued that capitalism is an ambivalent phenomenon. It is the overestimate of the

material cultural element or the overwhelmingly material culture which made a personality sacrifice that distinguishes a capitalistic culture (Sombart, 1902, 2:83–6). Sombart's antipathy toward capitalism is clear in his statement: 'There are no industrial sectors which remain untouched by the breath of capitalism. Worm is eating in all' (2:618). Nevertheless, the ultimate reason why he was convinced of the progress of capitalism was that the development of capitalistic small business as an art industry will ensure that an increasingly wider portion of the nation participates in the products of the art industry with a democratization of luxuries (2: 314–15). That is, Sombart expected that the overwhelmingly material culture would move toward a refined material culture and an artistic and unethical culture.

The second edition of Der moderne Kapitalismus

In the introduction of the second edition of *Der moderne Kapitalismus* Sombart emphasizes that the fundamental problem and the basic thought have not changed from the first edition. His argument regarding a conversion of the economic principle from the crafts to capitalism indeed has not changed, but it has been revised substantially both in methodology and in content. As its title indicates, this book is a genetic and systematic economic history of all Europe based on an ideal type. First, Sombart seriously considers the economic role of the state, which he completely ignored in the first edition, and second, he presents a pessimistic view about the future of capitalism. The former is a concession to Schmoller, whom he criticized, and the latter means that his inherent but romantic antipathy toward capitalism has become radical.

Early capitalism

Sombart considers the economic role of the modern nation-state on three levels: the preconditions, the promotion, and the hindrance of capitalism. He defines the state as an element of the institutional culture: the state, as well as the church, the economy, and customs, restrict the peculiar economic life (1916–27, 1:17). With this framework, Sombart explains the formation of both the capitalistic economy and the modern nationstate from the depths of the European mind. It is Faust's spirit or will to power that wants to break through the traditional barriers and extend itself infinitely in this world (1:327). The spirit of business enterprise, which is one part of the capitalistic spirit, is in this way reduced to a desire for power and conquest. The state and the economy come into existence from the common root and restrict and regulate each other (1:335).

Corresponding to such an understanding, Sombart adds state leaders, bureaucrats, and landlords to the entrepreneurial category. They are the

conquerors who control the means to power, just as the monarch is often the first entrepreneur of his people (1916–27, 1:842). As the representative of public society as a whole, the bureaucrat also contributes to dissolving the structure of the old society and promoting the construction of a new society (2:1097). In other words, here Sombart accepts the core of Schmoller's view of mercantilism, which stresses the decisive role of the state in the economy as it related to business enterprise in early capitalism. However, in Sombart, a source of the state's initiative is the desire for power in contrast to Schmoller, and the relationship between ethics and economic development is basically separated, as it was in the first edition.

In this way, Sombart introduces the state as the biggest driving force in the history of early capitalism. First of all, he asserts that the formation of the modern army as the collective army is a precondition of capitalism. It creates the opportunity for mass buying and mass production through the heavy demand for arms and regimentals; at the same time it is a suitable means for the expansion desire of the monarch (1916–27, 1:345). For Sombart, the state and its army are the original furnace of the revolution (2:511). Moreover, the monarch who aims to expand his interest to the state's interest develops a mercantilist policy as a joint enterprise with rising capitalism. The absolutist state, being the economic subject as an entrepreneur, promotes the capitalistic industries and large-scale foreign commerce (2:369).

Another factor that promotes capitalism is the private luxury of royalty and the nobility. The argument on luxury that Sombart presented for high capitalism in the first edition is now redirected as a factor promoting early capitalism. The two roots from which the capitalistic industry came into existence are demand for luxuries and the needs of the army. They became 'the main artery of the early capitalistic national economy' (2:862–3).

In spite of such development, Sombart holds that 'what [the early capitalistic period] brought about the advance of creative achievements in Europe, is surprisingly little when measured by today's standard' (2:1111). In his view, even at the end of the early capitalistic period, the old economic institution of agriculture was still continuing, but the crafts were finally beginning to be threatened.

Sombart assumes here that the organic character of the technique is the restraining factor of early capitalism as well as the war he had already mentioned in the first edition. Whereas the latter had a destructive influence on business activities, the former imposed limitations that increased the cost of production and transportation, as well as needing a vast area of agricultural lands and forest to supply food and raw material. Early capitalism could not totally conquer the dominant area of the self-sustaining economy and the crafts for such reasons (2:1134).

Sombart's understanding of the end of the early capitalistic period is basically unchanged from the first edition. But the hindrance that he

regarded merely as a restraining factor of the development in the first edition is further held to bring about the imminent end of capitalism here (2:1137). That is, the expansion of early capitalism and repeated wars exhausted forest resources through increased shipbuilding and mining, and threatened the continuation of civilization (2:1153). From an ecological viewpoint, Sombart emphasizes, the modern nation-state that once promoted capitalism is now bringing about the collapse of capitalism.

Sombart's argument on early capitalism in the second edition is an important attempts to develop Schmoller's mercantilism. He confesses a belief in mercantilism, and postulates that 'what Schmoller did for the mercantilist policy still has to be accomplished for the mercantilist theory' (2:912). But it can be said that Sombart pointed out the historical limits of mercantilism by introducing the ecological issue.

High capitalism

According to Sombart, the period of high capitalism broke through the crisis of early capitalism and made capitalism the dominant economic system. Control of economic life was no longer maintained by the state but had moved to the capitalistic entrepreneur (1916–27, 3:11), and an industrial society emerged, characterized by big business and the dynamic business cycle; the purification, secularization, and reification of the capitalistic spirit; the introduction of modern techniques and the mobilization of capital with the establishment of financial organizations; and so on. The era of high capitalism had the ability to create—for the first time— conditions to dissolve the precapitalistic and traditional economic system. At such a point, the basic thought of Sombart's second edition was the same as in the first edition. Nevertheless, his opinion of capitalism had changed enormously, and the antipathy to capitalism that he had suggested in the first edition he now emphasized at the beginning of the book. In capitalism, 'We know that…nothing of cultural importance has yet emerged and nothing will emerge [from it] in the future' (3:xxi). Then he intends to provide a favorable evaluation of the precapitalistic and traditional culture as opposed to his negative response to the capitalistic material culture.

Sombart tells us that in the high capitalistic period capitalism becomes the dominant economic system, but it is never the *only* one. In this period in which the peasant economy is self-sustaining, the crafts continue to function, and normative economic forms like the cooperative society and the collective economy develop (1916–27, 3:xvi). To explain why precapitalistic economic forms survive, Sombart presents his unique concentration theory that criticizes Marx. According to this theory, the rationalization of management progresses until management reaches an optimum size, but the optimum size differs among branches of the economy.

In the producer's goods sector and in a part of the textile industry, it is possible for big businesses to absorb smaller ones, whereas it is possible to allocate the economic activity widely among the large, medium-sized and small businesses in the consumer goods industry, commerce, and banking. In agriculture, the concentration movement does not exist, and, owing to the nature of the work, peasant management is predominant (3:817ff.).

There is also a technical reason why precapitalistic economic forms survive. According to Sombart, the expansion of management means its spiritualization [Vergeistung]; 'it is important to understand why and how management changes the society from a community of human beings who are mutually bound through personal relations into a system of artificially combined operations carried out by replaceable staff (3:895). In other words, the high capitalistic process is 'the dehumanization [Entseelung] of management' in which human relations become mechanized, such as Henry Ford's style of management. However, this tendency towards dehumanization has its limits. Particularly in agriculture, commerce, and the mining industry, success will never be possible without thinking human beings (3:917–18).

Sombart emphasizes that the crafts industry was maintained as a whole, and, at the same time, that internal reorganization was occurring and the capitalistic small entrepreneur was increasing in number (3:963ff.). The appearance of the capitalistic small entrepreneur, whom in the first edition he regarded as an indicator of the dissolving of the crafts, is here related to his concentration theory and presented as proof that small and medium-sized businesses could hold their own against big business. Thus, whereas in the first edition Sombart stressed that the crafts were dissolving as an economic entity, in the second edition he observes that the crafts continued and expanded into small and medium-sized businesses. Here he is critical of his first edition's argument that the art industry would develop as a capitalistic small business and admits that the refining of the taste, which should occur with its development, has not penetrated so deeply (3:597). He, therefore, should not have emphasized the dissolving of the crafts.

Sombart places greater importance on agriculture than the crafts, as he tends to disparage capitalism as a whole. In the opening of the second edition he highlights not the crafts but the self-sustaining economy and the peasant economy. In his view, agriculture was far less dependent on the market than capitalistic business and the crafts. In the agricultural sector, the influence of a uniformity or a unification on the market forces management to recede, and variable factors such as nationality, terrain, climate, and history play a more important role (1916–27, 3:970–1).

In the high capitalistic period, however, capitalism could not dissolve the precapitalistic economic systems. Besides, Sombart calls attention to the appearance of the cartel and the trade union, both of which bring about the end of free activity in the market (3:685). The decline of the market

that accompanies the expansion of big business and the stabilization of economic life through conscious regulation makes less room for reckless entrepreneurs (3:1013). This is symptomatic of a shift from high capitalism to late capitalism [Spätkapitalismus], in which Faust's spirit diminishes in the entrepreneur.

According to Sombart, although the capitalistic economic system will still dominate important sectors of economic life in the long term, the precapitalistic economic system will continue to expand, and the super capitalistic economy, such as the cooperative society, the collective economy, and the planned economy, will be added (3:1012). He recognizes that the difference between late capitalism and socialism is not so large, but he has no interest in whether the economy that is formed is capitalistic or socialistic. The problem for him is 'whether a place for…the self-sustaining economy, the crafts, and the peasant economy is found in the future economy as well as for the capitalistic economic system and for socialistic economic system' —in other words, 'whether the most important human act, i.e. economic activity, should belong to the sphere of soul [Seele] or the sphere of spirit [Geist] (3:1017).

The positive economic role of the state that Sombart attributed to early capitalism is confined to a subordinate one in the high capitalistic period. But, as his romantic evaluation of the precapitalistic economic system becomes strong, he will again assign the state the function of developing the sphere of the soul. For this purpose, he must reorganize his argument regarding the state, not from the viewpoint of the will to power but from the viewpoint of the romantic community. Then Sombart will want an authoritarian state, as he clearly demonstrates in *Deutscher Sozialismus* (1934).

Conclusion

Schmoller's social policy intended not merely to settle the problem of distribution among the social classes, but also to promote industry in Germany as a developing country so it could catch up with the more advanced nations. For him, economic progress meant an increase in economic rationality because ethics would penetrate the economy. Sombart rejected such an ethical viewpoint of history. In his view, economic development was driven by the profit-making motive.

In the process of revising the first edition of *Der moderne Kapitalismus,* Sombart certainly conceded to Schmoller's argument for mercantilism. At the same time, however, he denied the historical meaning of Schmoller's argument by rejecting a continuous relationship between early capitalism and high capitalism. Sombart's romantic anticapitalism and positive evaluation of the crafts and the peasantry give the impression that he has returned to Schmoller's protection of small business. But both arguments

have a historically different character. In the context of the Weimar period, when Nazism was coming to prominence, it would be overcompensation if Sombart, who started with an attempt to banish ethics from Schmoller's historico-ethical method (in contrast to Max Weber, who tried to reconstitute ethics as a historical cause), arrived in the end at a romantic evaluation of the peasantry and the authoritarian state.

Notes

1 See Appel (1992); Brocke (1992); and especially Lenger (1994).
2 For my detailed research on Schmoller, see Tamura (1993).
3 According to Priddat (1995, 33f.), 'the ethical' in Schmoller does not oppose economy but rather is dynamic as the investment in human capital.

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Chapter 8

Max Weber and the critical succession of the German Historical School

Kazuhiko Sumiya

The relationship between Max Weber and the German Historical School has recently been taken up as one of the main themes of studies on Weber. After World War II, Weber's image was influenced by the insistence on modernizing American social science, and the focus has shifted from history to sociology.[1] Along with this shift the significance of the above relationship to the study of Weber generally has decreased. But along with the rise in evolutionary and institutional economics in the United States, and also with the study of Weber's works ('Werkgeschichtliche Analyse'), which was initiated by F.H.Tenbruck's fundamental critique of the composition of Weber's *Wirtschaft und Gesellschaft,*[2] there has been a renewed interest in the German Historical School and especially Weber's relationship with that school.[3] The appearance of the *Max Weber Gesamtausgabe* [Complete Works of Max Weber], the publication of an epistolary collection and new materials regarding Verein für Sozialpolitik [German Society of Social Policy] have greatly contributed to this interest in Weber.

The Weber studies in Japan

In Japan, where studies of Weber have been conducted in economics all along, research has centered on his relationship with the German Historical School. Shiro Kawada's *Capitalistic Spirit,* brought out in 1910, may have been the first publication in a non-European country to treat Weber's work on the spirit of capitalism. There is no doubt that the circumstances under which Weber was first accepted by Japanese economists exerted a great influence on subsequent Weber study in Japan. The image of Weber as sociologist became predominant because of American influence on postwar social science. This was exactly the same as in Europe. However, Weber study in Japan has its own history of scholarly interest, even though it was greatly influenced by Europeans and Americans. We can recognize several streams. One is the acceptance of Weber's theory of the spirit of capitalism in the field of economic history initiated by Hisao Otsuka.[4] Since Marxism had a strong hold on the study

of economic history in Japan, Otsuka's favorable reaction to Weber necessarily produced a confrontation with Marxism; accordingly, Weber's image was formed on the uniquely supplementary relationship of Marx and Weber. Other research concentrated on Weber's personal history, beginning with Hideharu Ando's study of Weber as a man. Ando was influenced by 'Weber and Marx', written by Karl Löwith (Ando 1965). Ando's analysis forms one of the broad streams in current Weber study and overlaps another stream—that of Euro-American research focused on the development within his works.[5]

Research on the development of Weber's works came to focus on the question of what was the main purpose of his studies, discarding the traditional interpretations of *Wirtschaft und Gesellschaft* as his chief work. This led to inquiries regarding the relationship between 'Die Wirtschaftsethik der Weltreligion' [The Economic Ethic of World Religions] and *Wirtschaft und Gesellschaft*.[6] Questions were also raised about *Wirtschaft und Gesellschaft:* its relationship to the Historical School and its position in the history of German economics. As Otsuka's studies center on Weber as a social scientist rather than a man, they focus on how his scholarly achievements contributed to the development of the social sciences.[7] The problem of *Wirtschaft und Gesellschaft*, which emerged from the study of the development within his works, has now crossed the direction of study on Weber as a social scientist initiated by Otsuka. Conforming to the history of Weber studies so far performed in Japan, I deal with the problem of *Wirtschaft und Gesellschaft*: I discuss how it sheds light on the traditional theme regarding the relationship between the German Historical School and Weber.

Formation of universal historical perspective

Needless to say, the most famous writings of Max Weber are 'Die Protestantische Ethik und der Geist des Kapitalismus' (1904–5 and 1920) [The Protestant Ethic and the Spirit of Capitalism] (usually called the 'Essay on Ethic') and 'Die 'Objektivität' sozialwissenschaftlicher und sozialpolitischer Erkenntnis' (1904) ['Objectivity' of Social Science and Social Policy] (usually called the 'Essay on Objectivity'). The 'Essay on Objectivity', as Tenbruck pointed out, will be remembered for its critique of the *Methodenstreit,* i.e. the controversy between the leaders of the Austrian School and the German Historical School and for an implicit confrontation of Marxism that had exerted a strong influence on academic circles of the period.[8]

The 'Essay on Ethic,' in contrast, draws attention to the reason why he was obliged to abandon his research plans announced at the end of the Essay. He mentioned two reasons (Weber 1947:206). One was that Ernst

Troeltsch brought out his *Die Soziallehren der christlichen Kirchen und Gruppen* (Tübingen, 1912) [Social Teaching of the Christian Churches], and the other was that Weber decided to publish the results of comparative research on the universal historical relationship between religion and society and to place them within the entire frame of cultural development without isolating the religious Essays. Explication of the first reason—the relationship between Weber and Troeltsch—would require a context with regard to the broader stream of German historicism, which is beyond the scope of this chapter (Graf 1988). However, the second reason contains the notion of 'universal history' [Universalgeschichte] that is not found in the 'Essay on Ethic' published in 1904–5. If we recognize the possibility that Weber drafted his 'Soziologie der Musik' in 1910–12, as Schluchter says,[9] it is possible to seek the origins of the notion of universal history at the time Weber started to compile *Grundriss der Sozialökonomik* [Outline of Social Economics] (hereafter cited as G.d.S.) in 1909. Weber had accumulated the necessary research to shift his focus of study by this time. Two prominent achievements stemming from this research were 'Die Agrarverhältnisse im Altertum' [The Agrarian Sociology of Ancient Civilizations] in 1909 and 'Zur Psychophysik der industriellen Arbeit' [The Psychophysics of Industrial Labor] in 1908–9. Many Weber researchers in Japan have paid attention to the former. Eiichi Kaneko considers 'Agrarverhältnisse' to be an important treatise that serves as the dividing point between the first half and the second half of Weber's formation of social theory. But he placed this treatise in the last phase of the first period of Weber's scholarly work, first, because its theoretical part is not comprehensive and systematic like that of *Wirtschaft und Gesellschaft,* and second, because its historical description is more genetic compared with that of 'Wirtschaftsethik' and the method of comparison is not freely used as it is in the latter.[10] Whereas Kaneko's evaluation is based on the formation of Weber's interpretive sociology [verstehende Soziologie], Hideharu Ando takes a different approach and regards the motive of Weber's social theory as a pursuit of the process of rationalization. From this perspective, he deals with Weber's conception of modernization before and after his illness, the criticism of traditionalism, the struggle with mass society, and the theory of sect [Sekte]. Ando sees 'Agrarverhältnisse' as a work that enables us to understand the modern ages more comprehensively. This is because in this treatise Weber clarifies his viewpoint for both the Sociology of Domination and Economic Sociology, which were published at a later date. According to Ando, 'aristocrat vs. bureaucrat' is the basic theme of the Sociology of Domination, and the opportunity of markets to supply the public necessities of life is the viewpoint that supports Economic Sociology. In 'Agrarverhältnisse' the 'identification of time with space' in historical process is described in terms of 'change in geographical stage' from the Mediterranean Sea to the north of the Alps. Ando believes that if the 'identification of time with space' is

schematized, the world of *Wirtschaft und Gesellschaft* will be established. Given that Weber's interest extends to a global cultural comparison, the traditional descriptive method of history cannot cover all the facts, and there will be no other choice but to generalize on the basis of meaning. From this point of view, we can recognize the perspective of sociology in *Wirtschaft und Gesellschaft* that is characterized by the identification of time with space as a result of Weber's academic interest. Here research into the historical causal relationship becomes meaningless. Accordingly, Ando, unlike Kaneko, regards the work of agrarian sociology as an achievement that opens the second half of Weber's scholarly endeavors.[11]

Yoshiaki Uchida also appreciates 'Agrarverhältnisse' as a great achievement on the ancient economic history.[12] Although his argument is diversified into many respects, we should pay special attention to the fact that the root of his argument is Weber's theory of capitalism. His evaluation is as follows:

> Weber's academic interest was directly animated by the notion of universal history originated from the specific and individual observations of capitalism in modern European society. The direct purpose of his work 'Agrarverhältnisse' was, firstly, to examine the qualitative significance of ancient capitalism in comparison with modern capitalism, and to clarify the historical conditions of its social and economic aspects; secondly, to view the way of new development, specific to ancient Europe with 'oikos' economy, out of the process of falling ancient capitalism, and to identify a clue to the continuity of the whole process of subsequent European economic development. In other words, Weber's work examined both the fall of ancient culture (ancient capitalism and polis community) and the continuity of economic development from ancient times to the Middle Ages.
>
> (Uchida 1970:99)

Uchida also points out that Weber's perspective in 'Agrarverhältnisse' involves the whole ancient world including the Orient. According to Uchida, this treatise deals with the formation of rational ethics, comparison of 'pariah' capitalism with modern capitalism, comparison of ancient cities with those of the Middle Ages, family systems, 'oikos', and communities, etc. He refers to a schema of the comprehensive stage development of the ancient cities (ancient society) in the Introduction. We can say that Uchida connects 'Agrarverhältnisse' with the 'Wirtschaftsethik' on the basis of Weber's analysis of capitalism. His evaluation is the same as that of Ando, who regards the agrarian sociology as the starting point of the later Weber.

On the other hand, Hiroshi Orihara considers 'Agrarverhältnisse' as the extreme example of the study style based on the framework of the casuistic

theory construction and the specific historical description, and points out that the reconstruction of the framework constituted Weber's later social theory after his compilation of *Wirtschaft und Gesellschaft*.[13] His detailed examination is summarized as follows. Orihara's interest was originally directed to the study of *Wirtschaft und Gesellschaft* from the standpoint of the development within Weber's works, and he evaluated 'Agrarverhältnisse' also from this perspective. It is Johannes Winckelmann who insisted that the present edition of *Wirtschaft und Gesellschaft* consists of two parts, the first 'abstract and conceptual' and the second 'specific and substantial'. As is well known, it was Tenbruck who provided a comprehensive critique of this view from the point of view of the development within Weber's works. Orihara, after a minute analysis, agrees with Schluchter's criticism of both views. It is Orihara's opinion that *Wirtschaft und Gesellschaft* had already abandoned the idea of a 'two-part division' by 1914 and had shifted toward a 'single structure'. And he says that from this perspective the particular significance of 'Agrarverhältnisse' becomes more understandable; that the frame of the 'two-part division' emphasized by Winckelmann is most clearly observed in 'Agrarverhältnisse'. Orihara writes, 'this is a very reliable, complete work made in accordance with the "model of the two-part division" and a truly representative work of the "two-part division".' He continues:

> Since the evaluation is as such, I think, Weber reached the limitation of the 'two-part division' in this work.... When Weber wrote 'Agrarverhältnisse,' he realized the limitation indisputably by completion of the work. After 1910 he seemed to come to the general methodological policy (known as the 'distinction and integration of theoretical research and experiential research'—by Sumiya) that he should complete each research part separately.
>
> (Orihara 1988:141)

Although Orihara does not neglect the content of each work, his primary purpose is to analyze the chronological development within Weber's works, focusing on the relationship between *Wirtschaft und Gesellschaft* and 'Wirtschaftsethik.' As he evaluates 'Agrarverhältnisse' in this context, his analysis is very astute. I agree with Orihara that 'Agrarverhältnisse', as well as 'Zur Psychophysik der industriellen Arbeit', constitutes a watershed that divides the middle and later stages in the development of Weber's works. Nevertheless, up to the present time Weber researchers in Japan have not given the latter work the attention it deserves.[14] 'Zur Psychophysik der industriellen Arbeit' was a survey of actual conditions of industrial labor in Germany undertaken by Weber with his brother Alfred as a project of Verein für Sozialpolitik. It is important to note that it is the analysis of aptitude of skill which constitutes the subjective elements in productivity, while the ethos of labor is similarly a subjective element and discussed in

his 'Essay on Ethic'.[15] The psychophysics paper is a step in the 'conceptual revolution' that paved the way to the formulation of Weber's sociology of religion of later years, because it confirms the synchronic or panchronic meaning of 'factory management' (i.e. the rational organization of free labor) at a time when factory labor became a trend in the Second Reich (Küenzlen 1980:46–55) Then how was a bridge built for the next step to *Wirtschaft und Gesellschaft?*

Formation of casuistry: between the economic ethic of world religion and G.d.S.

Schluchter observes that the manuscript on the Sociology of Religion in *Wirtschaft und Gesellschaft* deals with the influence of social classes on religion, which had not been resolved in the 'Essay on Ethic', and with various characteristics of European culture. The manuscript was written based on the 'twofold function' that intended to grasp not only religion in relation to economic development, but also in relation to academic, artistic, and political development. Schluchter finds here Weber's shift of interest (Schluchter 1988:429). In this manuscript Weber indeed argues about the relationship between religious ethics and economic sentiment, which was the theme of the 'Essay on Ethic', but he gradually moves to other aspects of the world. Weber now holds a framework for recognizing the 'relative autonomy of the value spheres and the life orders, and the tensions and conflicts arising out of this state of affairs as well as their connection to rationalization strategies' (Schluchter 1988:430). The former interest obviously involves a historical approach—although from a typological viewpoint—in the sense that it is concerned about the mutual causal relationship between religious ethics and economic sentiment. In this sense, it is succeeding and expanding the theme of the 'Essay on Ethic'. However, the latter interest is not limited to the same level. On the contrary, it aims for the panchronic universal value par excellence. Along with the rise in the interest in value, the manuscripts contained in 'Wirtschaftsethik', especially the framework of the 'Einleitung' [Introduction] and 'Zwischenbetrachtung' [Intermediate Reflection] form the key themes of Weber's later years. On the other hand, the development of casuistry as the conceptual style for the analysis and clarification of parliamentary democracy, bureaucracy, and civil industrial management capitalism, which characterize modern European culture, provide the framework for the first part of the present edition of *Wirtschaft und Gesellschaft.*[16]

Of course, this is only a surmise. Nevertheless, we can find some signs that enable us to imagine the change or shift in the interests of Weber. For instance, in the footnote to 'Konfuzianismus und Taoismus', included in the first volume of *Gesammelte Aufsätze zur Religionssoziologie*, Weber wrote:

'the first part of the treatise was written two years ago, which I read to my friends and no revision was made…. In spite of this, the reason it was published without revision is that after the war, which meant a memorable event in their lives to all the people, I thought it was impossible to return to the stream of thought of the past.' (Weber 1947:237)

Undoubtedly the experience of World War I exerted a decisive influence on his stream of thought. It must have provided the opportunity for him to reconsider the meaning of human life and death. In 1915 his longtime friendship with Ernst Troeltsch finally ruptured over a difference of opinion concerning the permission needed to visit injured French soldiers in the military hospital Weber was in charge of. In this dispute we can see the conflict between nationalism and the universal values of human rights. Then in 1916, in a critical note 'Zwischen zwei Gesetzen' in *Die Frau*, which was concerned with the controversy between Gertrud Bäumer and Gesine Nordbeck on the love of motherland vs. the rule of the Gospel, Weber pointed out the eternal conflict between the God served by politics and the God of religion (Weber 1958:139–42). In this note Weber (p. 142) quoted from John Stuart Mill that if one proceeds from pure experience, one arrives at polytheism (this phrase reappears later in 'Wissenschaft als Beruf). Weber's experience of war awakened him anew to the grim reality that the world was in the maelstrom of 'Wars among Gods'. His first lecture expressing this deepened awakening—entitled 'Die Persönlichkeit und die Lebebsordnungen'—was delivered at a meeting of intellectuals and students at Lauenstein Castle in September 1917. He gave another lecture reflecting this viewpoint in science—entitled 'Wissenschaft als Beruf—in Munich in November 1917.

In 'Zwischenbetrachtung' published in December 1915, the conflict of value between intellectualism and the religious ethics is treated as an independent theme which has 'the greatest and the most basic significance', although it had not been an independent subject in paragraph 11 of the 'Religionssoziologie' manuscript concerning the conflict between the religious ethic and this world (Weber 1972:348–67). This seems to indicate the development of Weber's stream of thought after the manuscript in 1913–14.[17] In 'Einleitung' to 'Wirtschaftsethik', which was written in anticipation of the completion of the plan announced in the autumn of 1919, the evolutionalist conception of religion contained in the first, second, and third paragraphs of the manuscript of 'Religionssoziologie' not only disappeared but was also arranged in the direction of development typology. This may have something to do with the fact that the works in 'Wirtschaftsethik' are not based on the style of chronological description of history.[18] Relevant here is Troeltsch's remark on Weber in *Der Historismus und seine Probleme*: whereas Troeltsch was trying to understand historical development from a rational and teleological viewpoint, Weber firmly opposed this approach, and, in discussions with Troeltsch, called it a 'romantic delusion' (Troeltsch 1922:189–90).

Thus Weber was involved in writing monographs of universal history on the relationship between religions and societies in various cultures, on the one hand, and in constructing a casuistry of universal history concerning 'Economy and Social Orders and Powers', on the other. Through this endeavor he seems to try to eliminate 'historical thinking' in terms of stage theory from his historical-social theory.

It is generally recognized that the monographs of universal history in three volumes of *Gesammelte Aufsätze zur Religionssoziologie* are concerned with the cultural significance of a unique European phenomenon of rationalization, but the casuistry developed in the first part of *Wirtschaft und Gesellschaft* is different from the former manuscripts not only because it contains a lengthy second chapter 'Soziologische Grundkategorien des Wirtschaftens' that was not in the 1914 manuscript, but also because it is equipped with the conceptual apparatus necessary for the analysis of various cultural problems in advanced capitalism that are different from ones addressed by 'Wirtschaftsethik'. The examples of new concepts are: a modified version of Friedrich Knapp's monetary theory, and of the social theory of Ferdinand Tönnies and Georg Simmel,[19] a comparison of planned economy and market economy (including criticism of Otto Neurath), and a theory of capitalism in terms money and capital calculation. Furthermore, in chapter 3, 'Typen der Herrschaft', Weber discusses not only those problems that were dealt with in 'Wirtschaftsethik' such as patrimonialism, feudalism, and charismatic domination, but also new problems suggested by the political situation after 1917 such as collegiality, the division of power, parties, democracy, and representative system. These chapters represent the casuistry, based on the interest in universal history, to be applied to the analysis of contemporary economic and political issues.

The above observation not only agrees with Schluchter's view of the supplementary relationship between the universal historical monographs in 'Wirtschaftsethik' and the casuistry in the first part of *Wirtschaft und Gesellschaft*, the former approach consisting of the 'application of concepts' and widening of scope and the latter of the 'concept formation' and deepening of method. It also indicates the existence of a theme that is obviously outside the framework of the complementary relationship. Furthermore, the casuistry in the first part of *Wirtschaft und Gesellschaft* does not merely contribute to the creation of the universal historical monographs in 'Wirtschaftsethik', but also aims at the formation of the conceptual schema of 'Economy and Social Orders and Powers' required to analyze the development of the modern economy as the 'specific partial phenomenon of the general rationalization of life'. This was nothing but the original intention of the G.d.S.

Then it follows that the problem of *Wirtschaft und Gesellschaft* requires not merely the analysis of the development from his previous works (its relationship to 'Wirtschaftsethik'), but also the recognition that it possesses

its own domain that stands outside that relationship. Thus we can understand his persistence, as described by Marianne Weber in her biography of her husband. She tells us that until his death he meditated on various difficult concepts that are meaningless at a glance and attempted numerous modifications to the last. As she emphasized, the purpose of his casuistry was to present 'as clear, as objective, as universal recognition as possible of what was and what is, and above all, the greatest possible penetration of the forces of modern life' (Marianne Weber 1988:678).[20] And what manipulates the 'forces of modern life' [die Lebensmächte] is, according to the 'Introduction' to *Gesammelte Aufsätze zur Religionssoziologie*, capitalism, which Weber called the 'fatal force of the present age'. Therefore, we must reexamine the position of the G.d.S. that identifies the modern economy with the partial phenomenon of the general rationalization of life.

Weber the economist: a successor of the German Historical School

Max Weber is ranked equally with Emile Durkheim as one of the founders of sociology as a specialized subject. But we must remember that even though Weber was an important contributor to the establishment of the Deutsche Gesellschaft für Soziologie, he considered himself an economist concerned with economic theory and policy. In the controversy on value judgment in 1912–14, which he initiated, he presented his position as economist in 'Der Sinn der Wertfreiheit der soziologischen und ökonomischen Wissenschaften' (1917). His friend from their time together at Freiburg University, Gerhart von Schulze-Gaevernitz, regarded Weber as an economist to the last. Why is Weber regarded as an economist, not a sociologist, and how does this relate to the problem of *Wirtschaft und Gesellschaft*? Because, as seen above, this theme has been discussed only in the context of the research into the development within Weber's works and exclusively in relation to 'Wirtschaftsethik', it is profoundly important that we spotlight Weber as an economist who has been comparatively overlooked.

Needless to say, in considering Weber as an economist, the most important materials are the manuscripts of the lectures on economics that he gave at Freiburg and Heidelberg. At present we are not able to see all of them, but, fortunately, the reading guide and lecture outline for his lectures at Heidelberg in 1898 has been published under the title, *Grundriss zu den Vorlesungen über Allgemeine ('theoretische') Nationalökonomie*.[21] Since a detailed analysis of this guidebook is beyond the scope of this chapter, I will merely discuss the portions that relate to the theme of *Wirtschaft und Gesellschaft*.

The guidebook consists of an Introduction and six parts; the book is divided into twenty chapters. The first half of the book only presents the

contents of the lectures and a comprehensive bibliography; it is in the latter half that sentential description is presented, but it is confined to Part 1: 'Conceptual Basis of Economies' (chapters 2 and 3). The bibliography for the Introduction, entitled 'The Task and Method of Theoretical Economies' (chapter 1) lists the main works of the old Historical School such as those of W.Roscher, B.Hildebrand, and K.Knies and of the *Methodenstreit* between Carl Menger and Gustav Schmoller. Here we see that Weber in those days was interested in the *Methodenstreit*. The bibliography for the Introduction also contains other works such as the Modern Economics Handbooks from home and abroad, including Alfred Marshall's *Principles of Economics* (1891). Furthermore, it includes dictionaries, academic journals, and monograph series—e.g. *Schriften des Vereins für Sozialpolitik* (1873–).

The bibliography for Part 1 lists the chief works of Austrian School members such as Menger, Eugen von Böhm-Bawerk, and Friedrich von Wieser, and studies by Léon Walras (*Eléments d'économie politique pure,* 1889), and such classical economists as Adam Smith, David Ricardo, J.H. v. Thünen, and Karl Marx (*Das Kapital,* vol. 1) are recommended. It is noteworthy that the first volume of Marx's *Das Kapital* is listed often with pagination as required. Part 1 contains the 'Economy and Its Elemental Phenomena' (chapter 2) and the 'National Economy and Its Elemental Phenomena' (chapter 3), and these topics are explained in some detail in the second half of the guidebook. Here is a criticism of value theory of the classical school and socialism. The description of the theory of value indicates that Weber basically accepted the marginal utility theory of the Austrian School. It is essential to note that in the discussion on 'Assumptions of Abstract Economic Theory' in chapter 2 he sets a limit to Menger's theory. Weber states that 'this theory seeks, above all, to find the most elemental phenomena of lives of economically fully matured human beings', and the 'economic man' (homo oeconomicus) hypothesized by the Austrian School is surely a supposition of a methodical abstraction. But Weber adds, 'the abstract theory starts with the modern Western type of men and their economic behavior', and his explanation seems to conform to that of Marx in *Kritik der politischen Ökonomie* that the concept of 'labor in general' of the classical school arose from the abstraction from history. This is related to Weber's later statement in the 'Essay on Ethic' that the behavior of the Puritan (Quaker) of those days was, so to speak, the living law of the marginal utility (Weber 1947:191). This proves that he had in mind the theme of the 'Essay on Ethic.'

Weber maintained that the 'economic man' assumed in economic theory is a methodical abstract concept that focuses on the satisfaction of material wants as the sole motive of human beings. It is assumed that the economic man has the intellectual ability to grasp correctly the situation and economic rationality in choosing optimum means to achieve goals, and he is in endless pursuit of wealth. At the same time, Weber the historian observed that,

behind the fact that this methodical assumption was accepted as realistic as if it were generally appropriate empirically (the so-called problem of Adam Smith),[22] the development of modern capitalism was specific to Western Europe. The 'Essay on Ethic' is the result of the speculation about this theme, and the bridge from the 'Lectures on Economies' to the 'Essay on Ethic' had already been built and only crossing the bridge was left. For him to cross the bridge required further stimuli, the publication of G.Simmel's *Die Philosophie des Geldes* (1900) and Werner Sombart's *Der moderne Kapitalismus* (1902).[23]

In Weber's lecture guidebook, Part 2, 'The Natural Basis of Economy', includes the following chapters: 'Natural Conditions of Economy' (chapter 4), 'Population' (chapter 5), 'The Biological and Anthropological Basis of Society' (chapter 6), and 'The Relationship of Economy with Other Cultural Phenomena (especially Laws and the State)' (chapter 7). In chapter 7, H.W.Riehl's *Die bürgerliche Gesellschaft* (1851), F.Tönnies's *Gemeinschaft und Gesellschaft* (1887), and G.Simmel's *Über soziale Differenzierung* (1890) are noteworthy in light of his interest in later years.

Part 3, 'The Historical Basis of National Economy', consists of the following chapters: 'Typical Initial Stages of National Economy' (chapter 8), 'Economic Development of Mediterranean Culture' (chapter 9), 'Agricultural Basis of the Medieval Continental Culture' (chapter 10), 'City Economy and the Origin of Modern Enterprise' (chapter 11) and The Formation of National Economy' (chapter 12). Insofar as seen from the bibliography, Part 3 seems to depend on the achievements of German historical science and the Historical School of economics. Weber's later observation that 'Free Feudalism' existed only in Europe and Japan seems to originate from the description of feudalism in K.Rathgen's *Japans Staatshaushalt und Volkswirtschaft* (1891) listed in chapter 8. Chapter 9 covers the conversion of the ancient coastal culture to the medieval inland culture. As a supplement to chapter 9, he adds 'The Characteristics of East Asian and Ancient American Cultures'; it is interesting to note that this anticipates the comparative viewpoint that would be dominant in 'Wirtschaftsethik'. Chapter 10 reflects Weber's interest in contemporary arguments over the social system of the ancient German. Chapter 11 takes up Weber's own article, 'Zur Geschichte der Handelsgesellschaften im Mittelalter' (1889). His scheme 'from Hausgemeinschaft to Betrieb' concerns the origin of modern enterprises and is linked to the plan for *Wirtschaft und Gesellschaft*.[24] In chapter 12, with regard to manufacturing and the factory, Weber lists chapters 12 and 13 of the first volume of Marx's *Das Kapital*.

Part 4, 'Developmental Phases of Economic Theories', includes 'Economics before the Creation of Liberal Economic Theories' (chapter 13), 'Theories of the so-called Classical National Economy' (chapter 14), 'Theoretical Basis of Scientific Socialism' (chapter 15), and 'Recent Theoretical Trends' (chapter 15a). In chapter 15, Weber for the first time

addresses all three volumes of Marx's *Das Kapital*, along with Friedrich Engels's *Herrn Eugen Dühring's Umwälzung der Wissenschaft* (1878) and Böhm-Bawerk's *Zum Abschluss des Marx'schen Systems* (1895).

Part 5, 'Theoretical Analysis of the Modern Exchange Economy', contains 'Production and Its Theoretical Problems' (chapter 16), 'Exchange and Its Theoretical Problems' (chapter 17), 'Distribution, Consumption, and Their Theoretical Problems' (chapter 18), and 'Regulating Principles and Organization of Want Satisfaction through Exchange and Enterprise: Their Functions and Developmental Tendencies' (chapter 19). It covers problems of profit, rent, interest, wage, cartel, trust, depression, and unemployment. Under the section 'The Modern Means of Production in National Economy (Profit-making Capital and Wage Labor)' in chapter 16, he refers to the descriptions of 'the relative surplus-value and wage' in pages 245ff. and 469ff. in the first volume of Marx's *Das Kapital*; under the section 'Money' in chapter 17, he addresses the 'Fetishistic Character of Merchandise,' described in the same volume, pages 54ff. Furthermore, in 'Crisis and Unemployment' in chapter 19 he refers to the whole chapter on the 'Accumulation of Capital', including the process of primitive accumulation, in pages 459 to 688 in the first volume of *Das Kapital*, and in the section 'Capital Interest', he refers to pages 342ff. in the third volume. In the bibliographies Weber consistently provides page numbers of *Das Kapital*, indicating how he read Marx's work.

Finally, in Part 6, entitled 'Development and Analysis of Economic and Social Ideas' (also chapter 20), Weber cites Rudolf Stammler's *Wirtschaft und Recht nach materialistischen Geschichtsauffassung* (1896), which he would criticize in later years, and Sombart's 'Ideale der Sozialpolitik' (1897); he ends with his own inaugural address at Freiburg University (1895).

Based on Weber's guidebook, it is clear that he accepted the marginal utility theory of value and price, while he tried to construct the historical framework of the national economy in light of the achievements of the Historical School.[25] However, new wine requires new bottles. In Weber's mind, the conflict with the German Historical School began at this time. Before long it prompted his criticism of the Historical School's organic holistic view of the national economy in his essay on 'Roscher and Knies' (1902–6); it finally reached the 'Essay on Objectivity' and the 'Essay on Ethic'. In the 'Essay on Objectivity' he acknowledged the significance of the science of law for the abstract theory; however, he defined the boundaries of its application and insisted that social science should be the science of reality. Judging from this point of view, we may think that he succeeded to the insistence of the Historical School. Weber offered a theoretical solution to the so-called Adam Smith problem, i.e. the argument regarding the difference in human types, altruistic and egoistic—that was supposed to exist between Smith's two volumes *The Theory of Moral Sentiments* (1759) and *The Wealth of Nations* (1776) —by presenting the

ethos of harmony, which relates to the tension between economy and ethics, in terms of the spirit of capitalism. Now in front of him there appeared the horizon of a new social science.

In 'Zur Psychophysik der Industriellen Arbeit' Weber devised an analytic method for the market economy, in which the apparatus called factory exerted a profound influence on the technical skills of human labor. In 'Agrarverhältnisse', he approached the ancient world from the perspective of both the market structure (Economy) and the ruling structure (Society) and analyzed the historical conditions that affected economic development from the Middle Ages to modern times in Europe. These two works reinforce and supplement the 'Essay on Ethic' from two sides—current and historical analysis—and show that Weber overcame the theory of national economy (theory of capitalism) of the Historical School at every level of theory, history, and policy. Thus he started to compile G.d.S. in 1909. Tenbruck regarded it merely as busywork; however, from our point of view it is more reasonable to assume that it was more than that for Weber himself. I believe that in understanding this work, he thought that it would serve the 'new bottles' for a new social science. In those days the meetings of Verein für Sozialpolitik in Vienna saw confrontations between members of the old generation such as Schmoller and the new generation such as the Weber brothers. Weber, with Tönnies, Simmel, and others, made a strenuous effort to establish Deutsche Gesellschaft für Soziologie. We must consider the work of G.d.S. in relation to such circumstances.

His plan for G.d.S. indicates that he used the lectures at Freiburg and Heidelberg as the stepping-stone for the entire plan. There was a slight difference between the versions of 1909 and 1914, however. The plan of 1914 consists of five parts in nine volumes (Winckelmann 1986:202–5). The first part, 'Basis of Economy', is composed of three volumes: the first volume, entitled 'Economy and Economies', was guided by Karl Bücher (Developmental Phase of the National Economy), Joseph Schumpeter (History of Economics), Friedrich von Wieser (Theory of Social Economy). The second volume, 'Natural and Technical Relations of the Economy', covers economy and geography, population, consumption, and the division of labor, and contains Friedrich von Gottl-Ottlilienfeld's 'Economy and Technology'. The third volume is Weber's *Wirtschaft und Gesellschaft*. The above can be regarded as a revised compilation of the themes of the first four parts of the guidebook for the lectures. Then, the second and third parts in G.d.S. greatly expand Part 5 (Theoretical Analysis of the Modern Exchange Economy) of the guidebook, and the descriptions extend over another four volumes. The fourth and fifth parts in G.d.S. deal with the subjects that were not fully discussed in the guidebook, and show Weber's new perspective after the years at Heidelberg.

Thus G.d.S. can be said to represent an achievement that resulted from the knowledge that he accumulated over ten years and added to his

university lectures during that period. In his plan, the theory of national economy of the Historical School, which had emphasized organic holism, was transformed to the theory of the modern capitalistic market economy. This thought was already taking hold in Weber's guidebook. However, it is said that concerning the conceptual basis of the economy, Weber was not necessarily satisfied with the manuscripts of assigned contributors.[26] We can believe this given the many times he revised and rewrote the manuscripts of *Wirtschaft und Gesellschaft* for completing G.d.S. as a systematic whole. Minute research into this problem should be developed with the publication of his complete works. This chapter has only intended to demonstrate that Weber's *Wirtschaft und Gesellschaft* was derived from the critical succession of the German Historical School.

Notes

1 This was largely instigated by Talcott Parsons's *The Structure of Social Action* (1937). It is well known that American modernization was based on the so-called Weber thesis, which reportedly was influenced by Parsons.
2 Tenbruck (1977). The tremendous influence of his disturbing study extended to the publication of *Max Weber Gesamtausgabe.*
3 Pridat (1993,1995); Schefold (1989); Backhaus (1993); Koslowski (1994). In Japan a symposium on 'The World of the German Historical School', chaired by Kazuhiko Sumiya and Kiichiro Yagi, was presented at the meeting of the Society for the History of Economic Thought in November 1996. For the results of the symposium, see Sumiya and Yagi (1998).
4 Otsuka (1969–86). For his theoretical framework of 'Marx and Weber', see Otsuka (1966).
5 Orihara (1988); Yamanouchi (1998). Yamanouchi's work is noteworthy because of the role he played in shifting the theme of 'Marx and Weber' to the theme of 'Weber and Nietzsche' in the study of Weber in Japan.
6 Orihara (1996:2–15). Orihara aims to reconstruct the manuscripts according to Weber's plan in the years 1913–14, that appear in the second part of the present edition of Weber's *Wirtschaft und Gesellschaft,* compiled by J. Winckelmann. Winckelmann also criticizes Tenbruck's insistence that Weber's chief work is 'Wirtschaftsethik der Weltreligionen.' Winckelmann's intention is to restore the dominance of *Wirtschaft und Gesellschaft.*
7 For example, in economic history, the relationship between Weber's 'spirit of capitalism' and the formation of capitalism, the problems of the middle class in England, the significance of the concept of *Idealtypus* as a methodology of the social sciences, and the issue of community in the age of unmodernized society; in political science, Weber's sociology of domination including the traditional mode of domination, patrimonialism, especially charismatic domination; in the field of jurisprudence, his sociology of law centering around an ideological critique based on Marxian jurisprudence. The number of specialized fields that have been explored by Weber's theory is surprisingly large. See Amano (1972).
8 Tenbruck (1959:583–9). Tenbruck observes that Weber's 'Essay on Objectivity' is closely related not only to the *Methodenstreit,* but also to the new trend of thought (new idealism) at the end of the nineteenth century. But this issue deviates slightly from the theme of this chapter.

9 Schluchter (1988:417–18). Schluchter indicates that in 1909 Weber's religious-sociological program was not yet mature. He surmises that because 'Buddhistic contemplation', 'Christian ascetism of conviction', 'disenchantment', 'Nietzsche's theory of *ressentiment*', 'mystical contemplative', 'acosmism of love', and the 'role of the rational in history', which appear in the first, second, and third chapters of Weber's 'Über einige Kategorien der vestehenden Soziologie' published in 1913, are all treated in relation to the Introduction to 'Wirtschaftsethik', Weber's creation of the universal historical perspective reached maturity at that time. I think that Weber had another reason for compiling G.d.S. along with the formation of universal perspective in the sociology of religion indicated by Schluchter, and that relates to the theme of this chapter.

10 Kaneko (1957:19–20). The place of Kaneko's book in Japan is comparable to that of Abramowski (1966) in Germany.

11 Ando (1972:180, 231–2). Ando emphasizes that 'Agrarverhältnisse' is a decisively important treatise in the study of Weber (p. 119). This is because, compared with Weber's previous works, it bears a clear contradistinctive consciousness to ancient times (World of the Mediterranean Sea) and to the medieval and modern ages (Europe: north of the Alps); it is especially based on the awakening of European consciousness (Ando 1979:282).

12 Uchida's book (1970) does not intend to place 'Agrarverhältnisse' in the development within Weber's works, but evaluates its scholarly significance to the current study of ancient history. Accordingly, if we regard the quotation below as his complete evaluation, it may not be fair.

13 Orihara (1988:141). Orihara's critical comments on Winckelmann and Tenbruck are based on his minute analysis of the development within Weber's works. Basically his argument is similar to Schluchter's critique of Tenbruck, but is critical of the latter too. Orihara's study is unique, and I agree with many of his conclusions. For example, he rejects the view that *Wirtschaft und Gesellschaft,* including the draft written in 1914, is composed of two parts.

14 This subject has long attracted the attention of labor economics, and as a labor market survey was carried out extensively in Japan after World War II, Weber's article has been regarded as important pioneering research. Ujihara (1966), based on Weber, is a great achievement. Weber's survey was translated into Japanese by Hatsuo Tsuzumi under the title, *Industrial Labor Survey of Max Weber* (Tokyo: Japan Labor Association, 1975).

15 There are few works that analyze Weber's psychophysics paper in relation to his 'Essay on Ethic'. More attention should be paid to the fact that the 'Treatise on Ethic' recognizes the actual conditions of industrial labor in Germany in those days, and that Weber indicates that the psychophysics paper presents the grounds for his argument on ethic (Weber 1947:29). His wife Marianne immediately grasped the relationship between ethos and the form of technical labor (Marianne Weber 1988:367). In taking on the compilation of G.d.S., Weber obviously took account of the reality of German capitalism.

16 Schluchter presents an interpretation of integrating the two streams of thought as supplementary: one is monographic description of universal history in 'Wirtschaftsethik' and the other is casuistic formulation of universal history in *Wirtschaft und Gesellschaft*. In other words, he interprets the two in terms of the 'application of concepts' and the 'concept formation'. Taking this interpretation one step further, Orihara sees the two in terms of the division of labor between an empirical monographic work and a casuistic conceptual work, this style of research being found in Weber's works in his later years. Orihara as well as Schluchter view the two research styles as supplementary. I agree with

this view insofar as it relates to the development within Weber's works, but I think we should understand *Wirtschaft und Gesellschaft* in both the broader context of the development of German and indeed European social science and the narrower context of German development of the economic-social theory and the theory of economic and social policy.

17 As is well known, after 1914 the title of *Wirtschaft und Gesellschaft* was changed to *Die Wirtschaft und die gesellschaftlichen Ordnungen und Mächte*. However, if the viewpoint inherent in 'Wirtschaftsethik' addresses the relationship between religious ethics and other social orders, as evident especially in 'Zwischenbetrachtung', the methodical viewpoint of *Wirtschaft und Gesellschaft* can be expressed as concerning the relationship between economy and other social orders by replacing 'religion' with 'economy'.

18 In the 'Introduction' to 'Wirtschaftsethik' each religious ethic is treated as far more integrated than it appears to have been in history and is presented in the form of non-development and of logical consistency, which disregards the details of its complicated development (Weber 1947:267).

19 Although Weber evaluates Knapp's monetary theory, he does not discount the 'means of exchange' thesis that flows from classical economics. In the second chapter in the first part of *Wirtschaft und Gesellschaft,* he starts with money as the 'means of exchange' and recommends Ludwig von Mises's *Die Theorie des Geldes und der Umlaufsmittel* (1912). Regarding Tönnies's *Gemeinschaft und Gesellschaft* (1887), he transformed, for example, the concept of *Gemeinschaft* into the concept of *Vergemeinschaftung* as a behavioral concept. With regard to Simmel's *Soziologie* (1908), he refers to it from the same viewpoint in his note in the book margin.

20 Marianne's evidence has not attracted much attention so far. But the best possible attention is required.

21 Weber (1990). Tribe (1995: ch. 4) refers to this material, but we do not find anything in Tribe that traces the development from the 'Essay on Ethic' to *Wirtschaft und Gesellschaft*.

22 Lujo Brentano, who fiercely criticized Weber's thesis in the 'Essay on Ethic', attacked Smith's view of economic man *(homo oeconomicus),* calling it 'the dogma of egoism'. Cf. Brentano (1877:60–3). This criticism developed into an inquiry into the relationship between economic man and altruistic mind in *The Theory of Moral Sentiments* (1759) and resulted in the so-called Adam Smith problem peculiar to the Historical School. Regarding the summary of the problem, see Zeyss (1889) and Oncken (1898). In Japan Kazuo Okouchi (1943) refused to regard the relationship as conflicting in the split form 'economy vs. ethics' rather than in a unified form 'economic ethics'. Okouchi interpreted Smith's economic man similarly as Weber's 'Spirit of Capitalism'.

23 Immediately after Simmel's *Die Philosophie des Geldes* was published, Weber earnestly read it at a health resort in Italy (Marianne Weber 1988:252–3), and Weber's private holding of its second edition (1907), as Tenbruck indicated, contains many of his insertions (Tenbruck 1959:628–30). On Sombart, see Sumiya (1993). Weber's evaluation of Sombart went into reverse on the publication of *Der Bourgeois* in 1913. Until then, Weber had a high opinion of Sombart based on *Der moderne Kapitalismus* (1902) and other works.

24 The plan for *Wirtschaft und Gesellschaft* in 1914, according to Winckelmann, was to construct a large-scale 'Gemeinschaftstheorie' from 'Hausgemeinschaft' to 'Politische Gemeinschaft'. The posthumous manuscript on 'Hausgemeinschaft' contains two developmental strands from 'Hausgemeinschaft' to 'Betrieb' and also to 'Oikos'.

25 In later years Weber thought that it was possible to avoid a theory of value, and replaced the concept of national economy with the terms 'capitalism' and 'market economy'. Accordingly, the expression 'Nationalökonomie' was replaced with 'Sozialökonomik'.
26 Marianne Weber (1988:418–20). Weber was probably not satisfied with Wieser's *Die Theorie der Sozialwirtschaft*. Descriptions in chapter 2 of Part 1 of *Wirtschaft und Gesellschaft* overlap with those of Wieser, and we can surmise the above from the fact that for the economic theory he greatly values Mises's *Die Theorie des Geldes und der Umlaufsmittel*. The plan of 1914 did not include this long chapter. Weber probably tried to supplement Wieser's work, and this may be one of the reasons why chapter 2 became far longer than originally planned.

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Chapter 9

Joseph Schumpeter on the relationship between economics and sociology from the perspective of doctrinal history

Yuichi Shionoya

The leitmotif throughout the academic life of Joseph Alois Schumpeter was, in his own words, the research program of a 'comprehensive sociology'.[1] In his early work on the history of thought he predicted that the future direction of the social sciences would be their *'Soziologizierung'*:

> The substance of the new epoch is revealed by the tendency to understand as many things around us as possible—i.e. law, religion, morality, art, politics, economy, even logic and psychology—from sociology. The analysis of cultural phenomena is the lighthouse that the total fleet of different ships on different courses is headed for. And an epoch similar to the eighteenth century is approaching.
>
> (Schumpeter 1915:132–3)[2]

The eighteenth century was dominated by moral science or moral philosophy as the science of man. *Soziologizierung* for a reunification of the social sciences is the basic framework within which to understand Schumpeter's work. In fact, he did not develop a comprehensive sociology, but two sociologies—economic sociology and the sociology of science— that may be regarded as his strategic version of a comprehensive sociology. In this sense I have called the total body of Schumpeter's work a 'two-structure approach to mind and society'[3] after his discerning characterization of Giambattista Vico's work as 'an evolutionary science of mind and society' (Schumpeter 1954:137).

Integration of theory and history: reasoned history

In the *History of Economic Analysis* Schumpeter enumerated four basic methods of economics: theory, statistics, history, and economic sociology (Schumpeter 1954:12). Economic sociology, in contrast to the other three methods, goes beyond mere economic theory in the sense that it deals with institutions that are exogenously given in economic theory. Institutions are dealt with not only by descriptive history but also by economic sociology; the latter is defined as 'a sort of generalized or typified or stylized economic

history' (p. 20). In other words, economic sociology is the generalization, typification, and stylization of economic history by means of institutional analysis. This is what he often meant by 'reasoned history' (Schumpeter 1939, vol. I:220) or *'histoire raisonnée'* (Schumpeter 1950:44; 1954:690, 818).

At the outset several points with regard to Schumpeter's background in economic sociology should be noted. First, in his studies on the history of economics Schumpeter considered not only the development of economic statics and dynamics but also that of economic sociology. The analytic elements that he wanted to uncover in history were always those of economics and sociology. As the titles of his many articles show, he used both economics and sociology to analyze the overall nature of the problems in question.[4] Second, Schumpeter's conception of economic sociology intended to integrate history and theory, the antitheses at the *Methodenstreit* between Gustav von Schmoller and Carl Menger. The method of integration was to construct 'reasoned history' by means of the concept of institutions. Third, in Schumpeter's view, the source of economic sociology was the German Historical School. He appraised particularly the research program of Schmoller as a prototype of economic sociology and characterized its goal as 'a unified sociology or social science as the mentally ('theoretically') worked out universal history' (Schumpeter 1926:382). Schmoller's program of economic sociology, for Schumpeter, would eventually lead to a comprehensive or unified sociology. It follows that the key to understanding Schumpeter's basic view of *Soziologizierung* is found in Schmoller's research program.

Schumpeter, however, did not accept Schmoller's research program, both in its formal and substantive aspects, as it actually stood. In the formal aspect of the program Schumpeter characterized economic sociology as 'a specific discipline that, owing to the nature of its subject matter, is not only a detailed and fact-finding discipline but also a theoretical inquiry' (Schumpeter 1926:369–70). He emphasized the need to construct a theory rather than to be content with the mere collection, classification, summarization, and *ad hoc* explanation of historical data.

Schumpeter was also critical of the substantive aspect of the program. Among several distinct viewpoints of the German Historical School, Schumpeter took seriously two substantive elements: a belief in the unity of social life and a concern for development, a combination of which would explain the evolution of an economy involving interactions with non-economic spheres.[5] Instead, he rejected the school's claim that the relativity and individuality of historical experience would preclude general and universal theorizing of society. For him, the greatest significance of the method advocated by the German Historical School was the recognition that historical materials reflect the development phenomenon and indicate the relationship between economic and non-economic areas,

thus suggesting how the disciplines of the social sciences should interact in a historical context, with the economic area remaining the focus of investigation.

This recognition constituted his idea of economic sociology as well as a comprehensive sociology, because whereas economic sociology deals with the interaction between economic and non-economic areas, a comprehensive sociology is supposed to be a synthesis of interactions between every single area and all others. Therefore, when Schumpeter examined the few existing overarching systems of thought that had covered various aspects of society, he was interested in the relationship between economics and sociology within these systems.

Although Schumpeter did not explicitly develop a methodological inquiry into the relationship between economics and sociology, he did not hesitate to evaluate grand theories that involved economic sociology, unitary social science, universal social science, and the like, going beyond the boundary of economics. In what follows, I consider his writings on the grand theories in the history of thought in order to reconstruct his views on the method of an interdisciplinary social science. Because my analysis of Schmoller's research program as the prototype of Schumpeter's economic sociology is developed elsewhere (Shionoya 1997:200–7), I deal here with Schumpeter's views on the work of four major sociologists—Auguste Comte, Karl Marx, Vilfredo Pareto, and Max Weber—with regard to their methodologies of the relationship between economics and sociology. Schumpeter discussed them not only in his 1914 and 1954 studies on the history of economics but also in separate articles on each of them (except Comte).

Schumpeter's conception of economic sociology

In delineating Schumpeter's conception of economic sociology, we should examine more deeply the methodological significance of two elements that he made much of among the viewpoints of the German Historical School: the unity of social life and a concern for development. The perspective of the unity of social phenomena provides, as it were, a *horizontal* axis from which to observe a society that consists of various areas of social life. This perspective does not necessarily provide a dynamic view of society but a static view of interrelated social areas. To provide an accurate understanding of Schumpeter's conception of economic sociology, the horizontal axis must be combined with a *vertical* axis, which represents the viewpoint of the evolution of society. For Schumpeter, it is the observation of the historical process that integrates these two perspectives and makes economic sociology a genuinely evolutionary science. 'Reasoned history' should formulate the mechanism for the evolution of society as a whole through the interactions between various areas of society. In this sense

Schumpeter's evolutionism differs from the direction of current evolutionary economics, which concentrates on the economic area.

Indeed, Schumpeter's *Theorie der wirtschaftlichen Entwicklung* (1st edn 1912; 2nd edn 1926) provided an analysis of evolution based on entrepreneurial innovation, but it was limited to the economic area and did not address interactions with other aspects of society. As a next step of inquiry, Schumpeter argued in chapter 7 of the first German edition of the book (although this chapter was omitted after the second edition) that his dynamic economics must be expanded to economic sociology as an evolutionary science by constructing a larger theoretical structure covering the non-economic areas and by articulating a mechanism for interaction between the economic and non-economic areas (Shionoya 1997:32–43). *Capitalism, Socialism and Democracy* (1st edn 1942; 3rd edn 1950), his most comprehensive work on economic sociology, synthesized his earlier research on social class, imperialism, and the tax state.

Schumpeter was interested in grand theories; among others, he felt an affinity with those of Gustav Schmoller and Karl Marx, although he did not abstain from criticizing them. He praised Marx for integrating history and theory along the line of the German Historical School: 'He [Marx] was the first economist of top rank to see and to teach systematically how economic theory may be turned into historical analysis and how the historical narrative may be turned into *histoire raisonnée*' (Schumpeter 1950:44). Schumpeter added an intriguing footnote to this sentence, arguing that it was not incorrect to say that Marx set the goals of the Historical School.

In terms of the integration of history and theory, Schumpeter metaphorically contrasted the 'chemical' with the 'mechanical' approach (Schumpeter 1950:44). According to him, Marx mixed history with theory *chemically* in the sense that he introduced historical materials into the very argument that produces a theory, whereas most economists who deal with history use historical data *mechanically* to illustrate or verify a theory.

Schumpeter, however, was particularly critical of the 'monolithic' view, which explained social phenomena by a single factor, if it was based, as it were, on the chemical combination of history and theory. Thus he rejected a 'single hypothesis of the Comte-Buckle-Marx kind', which attempted to attribute the whole process of historical evolution to only one or two factors (Schumpeter 1954:811). As indicated below, this label is so broad that it includes both Hegelian intellectualist evolutionism and Marxian historical materialism. In contrast, Schumpeter was more receptive to Schmoller's 'pluralistic' approach and labeled his *magnum opus, Grundriß der allgemeinen Volkswirtschaftslehre* (2 vols, 1900–19) a 'comprehensive mosaic' (Schumpeter 1926:354). Therefore, in terms of the integration or mixing of the various aspects of society, Schumpeter metaphorically contrasted the Marxian single huge block of stone with the Schmollerian

mosaic pattern achieved by cementing together small pieces of stone, glass, etc., of various colors.

In sum, with regard to the attempts to integrate theory and history Schumpeter paid attention to the methodological aspects of economic sociology: horizontal versus vertical, mechanical versus chemical, monolithic versus pluralistic, and individualistic versus holistic. Identification of a grand theory in terms of these aspects will characterize the relationship between economics and sociology.

Between positivism and idealism

Before delving into the systems of the major sociologists, it is useful to take a look at Schumpeter's intuitive perspective on the German Historical School. In his early speculation on the history of social thought, Schumpeter made an interesting observation about the location of the German Historical School (Schumpeter 1915:70–81). Whereas in the seventeenth and eighteenth centuries the Enlightenment in Britain and France brought about the rise of social sciences based on rationalism, positivism, and universalism, historicism was formed in Germany under the influence of idealism as a critique of the Enlightenment. Schumpeter regarded Thomas Carlyle, Auguste Comte, and the German Historical School as a reaction to positivism and the Enlightenment in the social sciences that had occurred in the eighteenth century, and he located the Historical School at the midpoint between Carlyle and Comte. It is worthwhile to reflect on what this configuration means. Schumpeter wrote:

> On the one hand, this school, like the Romanticists, reproached barrenness and banality of theoretical analysis, praised the national spirit and the unity of personality, and demanded the revival of philosophical observations. On the other hand, however, this school proclaimed 'exact factual research' as its principle, as opposed to 'nebulous speculation.' Both directions cannot coexist.... Yet, when did a scientific program ever have logical unity?... This school floated at the same time both in the stream of reaction of philosophical volition against analysis and in the stream of reaction of positivism against philosophy.
>
> (Schumpeter 1915:75–6)

Carlyle, who was influenced by German idealism and Romanticism, opposed the Enlightenment and utilitarianism. It may sound strange to regard Comte as a reactionary against positivism and the Enlightenment, because he was the originator of the words 'positivism' and 'sociology.' But he represented the current of social thought that pursued synthesis in opposition to analysis. In fact, his intellectual activity started with a farewell to the eighteenth century.

Locating the German Historical School between Carlyle and Comte illustrates its dualism. On the one hand, the Historical School, like the Romanticists, criticized the methods of isolation and abstraction in theoretical analysis as unrealistic and sterile. On the other hand, like positivists, it attacked the ambiguous and empty philosophical speculations of idealists. The Historical School could maintain this dualism because it was endowed with both the capability to grasp unified social phenomena and the inveterate propensity for empirical observation. Its historical approach had given the school this unique endowment.

These three perspectives equally regarded history as crucially important, but differences exist between them with regard to the formulation of history and characterize their distinctions. Hero worship of Carlyle constructed history as biographies of individuals. Schumpeter referred to the remark of his teacher, Friedrich von Wieser, that 'sociology is history without names' (Schumpeter 1954:786). This is quite telling in polarizing Carlyle and Comte. Between them, historicism placed emphasis on collecting historical materials that would serve the source of inductive generalization. Thus we see here a spectrum with the degree of theoretical abstraction of history rising from Romanticism (Carlyle) to historicism (German Historical School) to sociology (Comte).

It is important to recognize that all three, in their own views, are located outside the boundary of natural scientific positivism, which believes in universal laws. When Schumpeter argued that the Schmoller school was not Comtist at all, he incidentally mentioned that 'as regards the economists who faced each other in the Battle of Methods, Menger, the theorist, was much more Comtist than was Schmoller, the historian' (Schumpeter 1954:418).

The Classical School of economics was an outgrowth of moral science to which Newtonian natural philosophy had been applied and had nothing to do with the Carlyle-German Historical School-Comte spectrum. As Schumpeter's attempt to cultivate useful contacts within the Historical School signified, as it were, a big leap from the positivist camp to the idealist one, he might be compared to Dr Faust selling his soul to the devil in exchange for knowledge and power. The task of integrating theory and history implied the uneasy question of how to link the idealistic spectrum with the positivistic one. The strategy of linkage seemed to debunk Comte's pseudo-positivism which opposed the historical approach, to skip the position of Comte on the idealistic spectrum, and to devise a kind of historical approach that was compatible with the theoretical approach on the positivistic spectrum. Economic sociology was expected to meet the requirements that Schumpeter imposed on the research program of the German Historical School. If Wieser called sociology 'history without names,' then Schumpeter called it 'reasoned history.' We begin our examination of Schumpeter's discourse on the relationship between

economics and sociology with Comte, with whom sociology had started and who put more stumbling blocks in the way of theoretical development than the Historical School.

Comte

Auguste Comte was an adventurer who launched into the organic unification of human knowledge in an era when the specialization of knowledge was inevitable. Schumpeter, who must have sympathized with such a project, treated him bitterly.[6]

Human societies, Comte argued, are fated to go through the theological, the metaphysical, and the positive stages of existence, and positive science develops in the order of complexity: mathematics, astronomy, physics, chemistry, biology, and, finally, sociology. Sociology, which would appear at the last stage of such evolution, was at first called social physics; it meant a science based on historical observation and was regarded as a universal human science at the positive stage. The hierarchy of science was based on the difficulty of observation, and the positive method had not yet been applied to complex social phenomena.

Then, what is the method of social physics? Comte thought that methods differ according to objects; that mathematics or a natural scientific method can be applied to the phenomena for which analytic isolation is possible; that since society is an organism that consists of interactions between parts, social physics or sociology requires a historical method to grasp society as a whole. There is no independent place for economics in Comte's scientific system, because, he argued, economics depends on the isolation and abstraction of an economy from society as a whole and indulges in useless metaphysical speculation.

British economists at the time reacted strongly to Comte's view. Their criticisms are recorded in the methodological writings of John Stuart Mill (1865), John Cairnes (1873), Alfred Marshall (1885), and John Neville Keynes (1917). Schumpeter in a similar vein argued that Comte's hierarchy of science was nothing more than a metaphysical enterprise in the philosophy of history. Furthermore, he criticized Comte's conception of the positive method: although it started with the recognition of natural and exact science, it denied, as did the German Historical School, the method of abstraction and isolation for social phenomena, and it made generalizations from unanalyzed historical facts. Schumpeter disparaged Comte's methodology as a 'comedy of errors' (Schumpeter 1954:418). In Comte's framework of science, natural scientific methods, starting with the tool of mathematics, are to be applied in sequence to different areas of research such as astronomy, physics, chemistry, biology, and sociology. Schumpeter wondered why this view of science could not be applied to the science of society, i.e. sociology. Schumpeter's criticism of Comte to this effect is consistent in his early and later writings.

There may have been a prejudice, like the hatred in kinship, in Schumpeter's critique of Comte. Unlike the British opponents of Comte, Schumpeter must have been distressed by a tension between the construction of an exact economic theory and the all-embracing grasp of society. He must have thought it inexcusable to deny the existence of theoretical economics by adopting a wrong method for the social sciences rather than develop an effective method of sociology. Anyway it is not possible for us to find a positive argument concerning the relationship between economics and sociology in Comte, who dissolved economics into sociology. In light of Schumpeter's rhetoric refuting Comte's sociology, his insistence on the autonomy of analytic economics is evident.

Marx

Part I of Schumpeter's *Capitalism, Socialism and Democracy* is devoted to an examination of the Marxian doctrine. It describes Karl Marx from four perspectives: as prophet, sociologist, economist, and teacher.

Schumpeter's discussion of 'Marx the prophet' deals with the teleological aspect of Marx and reveals Marxism as a religion that presented the goals of life and a guide to them and promised a paradise on earth. The religious quality of Marxism explained its success. Marxism not only advocated political slogans but also combined them with the positivistic and rationalistic mind. Furthermore, Marxism was an attempt at replacing the feelings of the masses with the alleged logic of social evolution. All in all, the success of Marxism was a combination of religionism, positivism, and historicism.

For just this reason, Marx's devotees found it outrageous to divide his work into pieces. Nevertheless, Schumpeter dared to separate it into 'Marx the sociologist', 'Marx the economist', and 'Marx the teacher' in order to sort out the valuable from the valueless in Marx's entire body of work.

In his assessment of 'Marx the sociologist', Schumpeter regarded Marx's sociological system as the historical interpretation of history or historical materialism and appraised it as one of the greatest achievements in sociology. He summarized it in the following moderate propositions: (1) All the cultural manifestations of a society are ultimately functions of its class structure, (2) A society's class structure is ultimately and chiefly governed by the structure of production, and (3) The social process of production displays an immanent evolution (Schumpeter 1954:439).

In Marx, the class structure of capital and labor is the axis of production relations; it governs the process of capital accumulation and exploitation of labor in relation to productive forces, on the one hand, and determines the superstructure including social, political, and cultural processes, on the other. In this sense, class structure is an important link between the superstructure and substructure of society, thus forming the monolithic system of economics and sociology in Marx.

Schumpeter criticized Marx's class theory for providing neither historical nor logical explanations because he believed in the success of innovation as the basis of social class formation. Schumpeter noted that arguing about the ownership of the means of production as the determinant of social class is as reasonable as defining a soldier as a man who happens to have a gun (Schumpeter 1950:18).

'Marx the economist' explains the mechanism of the substructure in a capitalist society, given the sociological concept of social class and the superstructure related to it. Schumpeter examined Marx's economic theories, including the labor theory of value, exploitation of labor, accumulation of capital, immiserization of labor, business cycles, etc., and concluded that all were defective in comparison with his own dynamic theory. Nevertheless, he admitted that Marx's economic theory was a truly great achievement:

> The grand vision of an immanent evolution of the economic process— that, working somehow through accumulation, somehow destroys the economy as well as the society of competitive capitalism and somehow produces an untenable social situation that will somehow give birth to another type of social organization—remains after the most vigorous criticism has done its worst. It is this fact, and this fact alone, that constitutes Marx's claim to greatness as an economic analyst.
>
> (Schumpeter 1954:441)

This remark indicates that Schumpeter did not accept any single economic theory of Marx but rather the total framework linking economics to sociology, although how to link them is the real problem.

By 'Marx the teacher' Schumpeter meant Marx's vision of structuring thought for an entire society. Its basic structure was the unity of economics and sociology in the sense that major concepts and propositions are both economic and sociological. Then it follows that:

> The ghostly concepts of economic theory begin to breathe. The bloodless theorem descends into *agmen, pulverem et clamorem*; without losing its logical quality, it is no longer a mere proposition about the logical properties of a system of abstractions; it is the stroke of a brush that is painting the wild jumble of social life. Such analysis conveys not only richer meaning of what all economic analysis describes but it embraces a much broader field…everything is covered by a single explanatory schema.
>
> (Schumpeter 1950:45–6)

In Marx's synthesis every factor is placed on the same analytic plane, and history, institutions, and politics—which are all outside the economy—are treated not as givens but as variables. In other words, Schumpeter explains

Marx's vision of a universal social science as follows: 'It is an essential feature of the Marxist system that it treats the social process as an (analytically) indivisible whole and uses only one conceptual schema in all its parts' (Schumpeter 1949:203). However, Schumpeter opposed Marx's method of synthesis. Because in Marx's system economics and sociology are one and are regulated by a single idea, there cannot be different *modi operandi* in economy and society or in the substructure and the superstructure, so that everything is reduced to the tedious theory of class conflict. 'A valuable economic theorem may by its sociological metamorphosis pick up error instead of richer meaning and vice versa. Thus, synthesis in general and synthesis on Marxian line in particular might easily issue in both worse economics and worse sociology' (Schumpeter 1950:46).

Schumpeter argued that cross-fertilization is likely to lead to cross-sterilization. With economics being self-limited, sociological aspects will rather stand out sharply in relief. In Marx's monolithic system of thought, no matter how all-encompassing it may be, sociological aspects are passively determined by production relations and lose their causal importance and independent roles. Schumpeter, the horseman, used a unique analogy in criticizing Marx's superstructure and substructure relationship: 'all the rest of social life—the social, political, legal structure, all the beliefs, arts, habits, and schemes of values—is not less clearly conceived of as deriving from that one prime mover—it is but steam that rises from the galloping horse' (Schumpeter 1949:204). Steam disappears in the air and does not affect the horse at all. If so, economists need not study mere epiphenomena lacking any vestige of autonomy.

Pareto

Vilfredo Pareto (1935) expanded the concept of general equilibrium in economics to that of 'social equilibrium' in a broad sense. His sociology deals with the interdependence between various elements in society as a whole and includes economics as a kind of science of interest. Distinguishing between logical and non-logical human actions, Pareto identified instincts and emotions as the determinants of non-logical actions and called them 'residues'. Residues are obtained through inductive research of reality. However, a justificatory inference to explain why non-logical actions take place is derived by logical and pseudo-logical deduction from a number of residues; Pareto called the result of this process 'derivations' or ideology. Thus he characterized his method as logico-experimental.

On the other hand, Pareto defined logical action in terms of subjective and objective consistency between ends and means. In his view, interest as the central concept of economics is not limited to the economic area but typically governs logical actions in various social areas. But for Pareto, far more important types of actions in society are non-logical, although they

are not illogical in the sense that they cannot be explained. The essence of Pareto's sociology is the analysis of complex social relations consisting of non-logical actions in terms of 'residues' and 'derivations,' or the elements of sentiments and the logic and rhetoric of justification.

At the same time, Pareto developed a theory of social class focusing on the rise and fall of elite classes that stems from conflicting types of residues in society. From the perspective of a social class theory, the social equilibrium represents a morphological balance between different groups, and a change in the composition of social classes means a shift in the social equilibrium. Therefore, in his sociological investigations, the four major determinants of social equilibrium are residues, derivations, interests, and social classes.

How can the visions of Pareto and Schumpeter with regard to the construction of a universal social science be compared? Specifically, how can the relationships between economics and sociology propounded by the two authors be compared? Both have several points in common: a social equilibrium based on general interdependence, a distinction between logical and non-logical actions, a difference between the elite and the masses, and the circulation of the elite.

However, their methods of the construction of social science are different. First, in Pareto's comprehensive sociology, economics or the science of logical action is a small subsystem to be embedded in the major framework of the analysis of non-logical action, because whereas economics only explains a theoretical equilibrium, sociology gives a concrete equilibrium of society. In other words, economics has developed an abstract theory not directly applicable to concrete social phenomena without synthesis with sociological elements. In contrast, the object of Schumpeter's universal social science is divided into economic and non-economic areas. These areas are not based on the logical-non-logical distinction nor on the sub-super distinction; rather, each area is characterized by the statics-dynamics distinction. Schumpeter treated the dynamic interactions of a social system not on a Walrasian general social equilibrium but on the Marxian dichotomy between the superstructure and substructure of society.

Second, Pareto did not address theoretically as well as empirically the concrete relationship between the economic and non-economic areas, nor did he clarify the place of social class theory within the framework of a comprehensive sociology. His theory of elite circulation remained an abstract idea based on the conflict between innovative and conservative residues. Schumpeter integrated the two areas on a sociological dimension, and his concept of social classes played the role of integrating various areas of social life. Because social classes in Schumpeter's theory had a historical dimension, he could write a scenario of the failing capitalist system on the basis of the ideological gap between entrepreneur and bourgeoisie. Pareto, in contrast,

made a general study of human society, whose universal nature has been historically repeated.

In view of Schumpeter's 'two-structure approach to mind and society,' it is remarkable that Pareto's *Trattato di Sociologia generate* was actually called *The Mind and Society* in the English translation. In terms of the three corners of Pareto's famous triangle relating to residues *(A),* actions *(B),* and derivations *(C),* the relationship between *A* and *C* belongs to the world of the mind, whereas *B* considers the world of society. For Pareto, social equilibrium depended on the interaction between mind and society, which was addressed by a sociology of knowledge and a sociology of class circulation. It is in this sense that Schumpeter found two different analytic frames in Pareto's sociology: social psychology and social morphology (Schumpeter 1951:136–41).The frame of social psychology deals with the function and structure of 'derivations' or ideology, whereas that of social morphology focuses on the dynamics of social classes. Pareto's two frames can be compared to Marx's superstructure and substructure of society. From this perspective Schumpeter observed that if Pareto had explained the derivation process in terms of class interests, and if he had defined class interests in terms of class status in the production system of society, then the theories of Pareto and Marx would have been similar.

In fact, however, Pareto interpreted the psychology of instincts and sentiments as abstract residues and was concerned only with the nature and function of theory or ideology derived from them. As a result, his analysis of the ideology of the elite was disconnected from social dynamics, which should have been developed within the morphological frame. In terms of Schumpeter's approach, his comment on Pareto means that there was no link between the morphological and psychological frames. It followed, according to Schumpeter's final remark, that Pareto's sociology was not of the first rank.

Weber

As Weber's contributions to the methodology of science and the wide range of sociology are regarded as a partial solution to the problems raised in the *Methodenstreit,* it is illuminating to compare his work with Schumpeter's. Apropos of the methodology of science, Weber's 'ideal type' is similar to Schumpeter's instrumentalism, although the philosophical sources of their thought—Weber's neo-Kantian origins versus Schumpeter's Machan origins—were different (Shionoya 1997:207–22). With regard to their work in substantive fields, Weber's sociological approach is comparable to Schumpeter's economic sociology. Both are viewed as an attempt to integrate theory and history, based on their scientific methodologies, within the broader concept of *Sozialökonomik* consisting of theory, history, and economic sociology, although Weber's approach extended beyond the economy, to law, politics, religion, etc. As far as

Weber's economic sociology is concerned, Schumpeter was right in identifying it with an analysis of economic institutions (Schumpeter 1954:819).

Our problem here is to determine Schumpeter's view of Weber concerning the relationship between economics and sociology. In an essay on his death, Schumpeter paid the highest tribute to Weber's work (Schumpeter 1920). But he consistently viewed Weber as a sociologist who was only indirectly and secondarily concerned with economic theory. In fact, according to Weber, the agenda of *Sozialökonomik* was to start with the general aspects of an economic phenomenon, then to go to the concrete historical facts, and finally to ascertain its cultural significance. The last stage of the agenda has much to do with the task of economic sociology. In Weber's economic sociology, economic activity is seen from a sociological perspective that focuses on the understanding of its meaning through application of the so-called interpretive sociology. This attempt produced a series of sociological categories that differed from economic ones. In this sense, Weber's economic sociology is not a monolithic construct of the 'Comte-Buckle-Marx kind', which does not differentiate between economics and sociology.

For Weber, sociology was a universal theory or discipline that could be applied to all areas of social life, and the results of such applications were specific types of sociology: economic sociology, religious sociology, legal sociology, and so on. On the other hand, Weber contrasted sociology with history. According to him, although both sociology and history are all-encompassing descriptions of society, history is concerned with the causal explanation of individual actions, groups, and personalities, whereas sociology tries to formulate type concepts and generalized patterns of the historical process. Sociology is thus a universal as well as a general theory that explains social and historical phenomena.

Schumpeter's criticism of Weber is largely wide of the mark. Apart from his critique of the neo-Kantian flavor in Weber's methodological work, his analysis of Weber's economic sociology focuses on the alleged confusion between a theoretical hypothesis and an explanatory hypothesis in the use of ideal types when he writes about Weber's 'fundamental methodological error' in *The Protestant Ethic and the Spirit of Capitalism* (1905):

> This method of (logically) Ideal Types has, of course, its uses, though it inevitably involves distortion of the facts. But, if forgetting the methodological nature of these constructions, we put the 'ideal' Feudal Man face to face with the 'ideal' Capitalist Man, transition from the one to the other will present a problem that has, however, no counterpart in the sphere of historical fact. Unfortunately, Max Weber lent the weight of his great authority to a way of thinking that has no other basis than a misuse of the method of Ideal Types.
>
> (Schumpeter 1954:80)

Schumpeter meant that Weber confused ideal types with historical concepts and used them directly for historical description. But it is fair to say that Weber was careful not to confuse ideal type with historical reality (Weber 1949:106–7). This methodological discussion may throw light on the nature of Schumpeter's famous thesis on the decline of capitalism. For him, the thesis was not historical but a theoretical hypothesis in economic sociology.

Schumpeter did not examine the whole system of Weber's sociological work. Whereas the methodologies of Schumpeter and Weber reveal many similarities, there was a big difference in the substance of their economic sociologies. Weber's sociology was much more concerned with comparative static social systems than with the dynamic process of evolution, or, as it were, with a horizontal axis rather than a vertical axis of society. Weber's analysis of the relationship between economic and non-economic areas remained static, as exemplified by the conformity between the Protestant ethic and capitalism. This may explain why Schumpeter felt more of an affinity to Marx and Schmoller.

Conclusion

From these observations we can attempt to reconstruct Schumpeter's stance about the relationship between economics and sociology more clearly than from an examination of the little he wrote directly on this topic.

First, Schumpeter believed in the autonomy of economics and opposed the holistic and organic method of Comte, which diffused economics into sociology, the so-called queen of the social sciences. This criticism also applied to Marx, one of the proponents of the 'single hypothesis of the Comte-Buckle-Marx kind'. From this perspective we are left with what might be called a varying hypothesis of the Pareto-Weber-Schumpeter kind, which admits the coexistence of economics and sociology and allows plural courses of causation between various aspects of society.

Second, for Schumpeter, Marx's monolithic approach to economy and society was separable into economics and sociology by drawing a line between the substructure and superstructure of society, Marx's key concepts in his economic interpretation of history. Given Marx's unilateral influence of the economic structure on the ideological superstructure, there is no need to inquire into the superstructure whose economic significance is nil. In contrast, Schumpeter transformed Marx's doctrine of historical materialism into economic sociology and focused on the bilateral relationship between economic and non-economic areas, or between the economic mechanism and the *Zeitgeist*. In particular, the Pareto-Weber-Schumpeter model commonly advocated the influence of mind on society.

Third, both Pareto and Weber put forward a sociological theorizing that was distinct from, but did not replace, an economic theorizing based on the narrow sense of rationality. However, their sociological approaches that

can be integrated with economic theory are very different. Pareto's sociology, the study of non-logical actions in terms of human instincts and sentiments, provided an analysis of a social system, to which economics gave an exposition of a subsystem. As seen below, according to Schumpeter the relationship between economics and sociology in Pareto was not so significant that Pareto's sociological system did not explain the evolution of society as a whole.

Weber's sociological method, which mainly addresses rational actions and is applied to all areas of society, consists of three basic concepts: order, organization, and institutionalization (Shionoya 1996:56–9). Thus, for Weber, economic sociology was an analysis of the institutional structure of the economy that explained its foundations in terms of individual orientation to an order. This thought process can be seen as an extension of Pareto's view on residues to include their influences not only on human actions but also on social institutions. Weber's study of Protestant theology encompassed not merely religious sociology but also economic sociology in that it explained the motivational structure that predisposed individuals to an orientation to work and rational action.

For Schumpeter, the use of the *Zeitgeist* or social psychology to show the impact of institutions on the economy, as illustrated in his thesis of the fall of capitalism, corresponded to Weber's sociological apparatus explaining the rise of the economic ethos in modern capitalism through the rational ethics of ascetic Protestantism. Weber's sociology was a substitute for Marx's one-sided approach to the relationship between economy and society. But it was not so much concerned with social evolution as with comparative social systems, and Marx's apparatus was required for an evolutionary perspective.

From a comparative perspective in the history of thought, Schumpeter's idea of economic sociology emerged out of German historicism and gained a stimulus consciously or unconsciously from Marx and Weber. Schumpeter's analysis of the relationship between economic and non-economic areas through the concept of social class was clearly an adaptation and a transformation of Marx's historical materialism. On the other hand, when Schumpeter tried to elucidate changes in institutional surroundings and their impact on economic activity, he attached importance to the rationality *Zeitgeist* in Weber's sociological work. In short, Schumpeter's economic sociology was an attempt to flesh out the two dominant viewpoints of the German Historical School—social unity and development—with Marx's analytic form and Weber's analytic content.

Notes

1 In a 1944 interview, Schumpeter called his long-standing research program a 'comprehensive sociology' and noted: 'All my failures are due to observance of

this program and my success to neglect of it: concentration is necessary for success in any field', *Harvard Crimson,* 11 Apri 1944.

2 This book is an expansion of his lecture on leaving the University of Czernowitz in 1911. It can be argued that Schumpeter's early studies on economic thought consisted of *Epochen der Dogmen- und Methodengeschichte* (1914) and the 1915 book; the former dealt with economic theory and the latter with the social sciences, including sociology.

3 By a two-structure approach to mind and society I mean the three-storied structure of economic statics, economic dynamics, and economic sociology, on the one hand, and that of the philosophy of science, history of science, and sociology of science, on the other (Shionoya 1997:260–5).

4 E.g. 'Economics and Sociology of Distribution', a section title of Schumpeter (1916–17); 'Economics and Sociology of the Income Tax' (1929); 'Economics and Sociology of Capitalism', a section title of Schumpeter (1946); and 'The Communist Manifesto in Sociology and Economies' (1949).

5 Schumpeter summarized six basic viewpoints of the German Historical School: (1) a belief in the unity of social life and the inseparable relationship among its components, (2) a concern for development, (3) an organic and holistic point of view, (4) a recognition of the plurality of human motives, (5) an interest in concrete, individual relationships rather than the general nature of events, and (6) historical relativity (Schumpeter 1914:110–13).

6 Schumpeter discussed Comte in Schumpeter (1915:73–5); (1954:415–18).

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Chapter 10

Lujo Brentano, Alfred Marshall, and Tokuzo Fukuda

The reception and transformation of the German Historical School in Japan

Tamotsu Nishizawa

Tokuzo Fukuda (1874–1930), a great pioneer of modern economic thinking in Japan, published his last work, *Welfare Economic Studies* in 1930, just two months before his death at the age of 56. In the introduction, he commented on the state of the economics profession in Japan: 'It is said that economics has reached a deadlock. Often we hear voices proclaiming the ruin of the German Historical School or the bankruptcy of the marginal utility theory. But among my fellow scholars, not a few have cast their eyes towards the quickly taken escape routes of Marxism or, especially, historical materialism'. Further, other people called for and rushed to accept new principles, such as the institutional school and behaviorism popular in America, Douglasism or new liberalism in Great Britain, or, from continental Europe, Schumpeterianism, the functional theory of Gustav Cassell and others, as well as Othmar Spann's universalism or Max Weber's idealism. Fukuda could pay no heed to any of these, nor hold out great expectations for the mathematical research of Léon Walras, Francis Edgeworth, Vilfredo Pareto, and Irving Fisher, whose work had not, he believed, progressed far. Therefore, he stated: 'The only course left to me is to move forward on the thorny trail of welfare economics forged by our teachers Hobson, Pigou, and Cannan' (Fukuda 1930:3–6).

Although he studied the works of Alfred Marshall and A.C.Pigou, it was particularly from J.A.Hobson that Fukuda had learned a great deal about welfare economics. His reaction to Hobson's *Wealth and Life* (1929) and Edwin Cannan's A *Review of Economic Theory* (1929) —'I can't stop being happy' (pp. 3–4) —expressed his belief that they were moving in the same direction as his own recent work. *Welfare Economic Studies* was, in fact, planned by Fukuda as a tribute to his master teacher, Lujo Brentano, who in 1929 was almost 85 years old. Fukuda wrote, 'From the very beginning, I had more or less similar thoughts on welfare economics.' As Ichiro Nakayama (1898–1980), who studied under Fukuda and Joseph Schumpeter and would become highly influential in postwar government policy-making, argued in the article 'Welfare Economics and Tokuzo Fukuda', published in 1978 to commemorate the hundredth birthday of his mentor, Fukuda's

ideas on welfare economics and his focus on labour issues can be traced back to his first work. *Labor Economics,* which appeared in 1899 and was written under Brentano's guidance (Nakayama 1978:59–77). This chapter explores Fukuda's thinking on the relationship between the German Historical School and the field that Fukuda variously called welfare economics or social policy.

Brentano and Fukuda's *labor economics*

Fukuda (1929a) once wrote, 'When I was a student at the Higher Commercial School in Tokyo, I often prayed that I would be able to attend a lecture by [Wilhelm] Roscher just one time'. Directed to study commercial science for three years overseas, Fukuda arrived in Leipzig on 5 May 1898. By that time, Roscher had died, so Fukuda studied instead under Karl Bücher. In the fall he transferred to Munich, and became a student of Lujo Brentano. Fukuda submitted his dissertation 'Die gesellschaftliche und wirtschaftliche Entwicklung in Japan' in 1900, but, more important, he and Brentano had coauthored *Labor Economics,* which was published in 1899. This volume was comprised of Brentano's translated writings and Fukuda's very substantial introduction. Its purpose was

> to introduce the ideas of my mentor Dr Brentano on recent labor theory, especially regarding the relationship between working conditions and productive capability, for learned people in Japan; to enable us to conduct more detailed comparative theorizing on our own real conditions; and to advance research on whether labour in our nation is as labor is believed to be in the Western countries, or whether it is, in fact, exceptional.[1]

Fukuda, citing John Rae's *Eight Hours for Work* (1894), explains that there is a tendency for fuel, machines, and other factors of production to become quite similar in all countries. It is only labor productivity that, owing to national differences, does not easily converge. From now on, the most important factor in global competition is labor productivity. Because other factors of production tend to converge worldwide, those countries that utilize it most skillfully will succeed in the global market. Skillful utilization means none other than 'having workers made strong and intelligent so that they are well endowed with productive capabilities'; the only way to raise labor productivity is to improve working conditions. Presenting this message was the reason for introducing the theories of Brentano on the connection between labour productivity and working conditions to a learned audience in Japan (Brentano and Fukuda 1899:2314–15).

In writing 'Über das Verhältniss von Arbeitslohn und Arbeitszeit zur Arbeitsleistung', Brentano researched British labor issues to provide a

comparative analysis with Germany. He believed that, to become as prosperous as Britain, Germany would need to raise wages and shorten working hours; thus he sought to prove that high wages and reduced working hours were linked to high labor efficiency.

According to Brentano, the most important issue in the social reform then taking place was the creation of unions and labor laws to protect the economic interests of workers. There were people who fervently supported such measures, but there was also strong opposition. He wrote, 'It is feared that labor organization and labor protection laws will raise production costs by raising wages and reducing working hours, so that domestic industries would lose selling power in world markets'. Brentano sought to demonstrate that improved working conditions would not undermine international competitiveness. To show that 'high wages are synonymous with high productivity', he first drew on the historical economic theories of Adam Smith to argue that higher wages and shorter working hours led to increased productivity, and next made use of empirical works such as Schulze-Gaevernitz's analysis of conditions in Britain's cotton industry and J.Schönhof's *The Economy of High Wages* (1892), a comparison of American and European industry.[2]

In opposition to the mainstream of the statist social policy theory, which emphasized redistribution, Brentano emphasized fostering improvements from the bottom up through labor unions, and he expounded his social liberalism and his 'production policy'-oriented social policy theories in his *Die Arbeitergilden der Gegenwart* (1871–2). Beginning by mastering the available information on British trade unions, primarily in the cotton-spinning industry, he found that wages in Britain were twice as high as in Germany, and Britain's working hours were nine compared with Germany's eleven. Brentano argued that Germany's labor efficiency came nowhere near to matching Britain's because its working hours were extremely long and its wages half those of Britain. Therefore, he argued, the only reliable course for achieving economic progress was to raise wages and shorten working hours to levels comparable to those in Britain in order to raise labor efficiency.[3]

In his 1978 tribute to Fukuda, Ichiro Nakayama, who has made a great contribution to the reformation and improvement of labor-management relations in postwar Japan as chairman of the Central Labor Commission and the Labor-Management Joint Consultation Committee of the Japan Productivity Center, praised Fukuda's *Labor Economics* as a pioneering achievement in dealing with an issue that had finally arrived in Japan. According to Nakayama (1978:64–7), whether or not to introduce higher wages and shorter working hours was a question dating from the previous century and one that Japan would have to face, under new circumstances, in the 1970s and beyond. In fact, Nakayama's 'Proposal for doubling wages' (1959) is said to be the intellectual basis of Prime Minister Hayato Ikeda's

national income doubling policy. Thanks to Fukuda, the first issues undertaken by the field of welfare economics were concerned with labor problems. Fukuda's ideas on welfare economics were drawn from the real, rather than the abstract, problems of labor.

The German Historical School, Marshall, and Fukuda

The German Historical School and Japan

The overseas study of promising young students like Fukuda and Hajime Seki (1873–1935) took place during the peak of the international movement to establish higher commercial and business schools—for example, Handelshochshulen in Germany, Faculties of Commerce in Britain, and Business Schools in America. In fact, the institutionalization or professionalization of political economy had just started. In a sense it was taking place in the course of the internationalization of the German Historical School. Seki studied with and was highly influenced by Gustav von Schmoller and Adolph Wagner in Berlin; it was about the time of Schmoller's publication of the first volume of *Grundriß der allgemeinen Volkswirtschaftslehre* (1900–4), which Seki read in Berlin as soon as it appeared and he wrote down his impressions in his diary. On returning to Japan in 1901, Fukuda and Seki proclaimed the necessity of producing 'captains of industry' and began to disseminate ideas on 'the new economies' of the German Historical School.

Fukuda began a series of lectures on comparative economic history in November 1901. While attending Fukuda's lectures, Teijiro Ueda (1879–1940), who would study under W.J.Ashley at the Faculty of Commerce in Birmingham and be a great pioneer of business economics in Japan, became enthused with the idea of being 'taught Schmoller-like theories of enterprise development' and was attracted by the German Historical School's explanations of how progress could be discerned even in economic life. The new work prompted Ueda to comment, 'With a feeling of true surprise, I welcomed and praised these novel thoughts.' Later, stimulated by his contact with Fukuda and Yoshio Takimoto (who studied at Berlin, was highly influenced by Wagner, and would break new ground in financial studies in Japan) and under Fukuda's guidance, Ueda read Schmoller and Bücher voraciously. This first decade of the twentieth century was 'the most important period in the building' of economics studies at Hitotsubashi University, and Fukuda's lectures on economic history lay at its heart. Fukuda first focused on the works of Brentano, Ashley and William Cunningham.[4]

According to Seki's 'Memoire', during his postgraduate program at the Tokyo Higher Commercial School (1895–6), Fukuda said, 'My close reading of [Wilhelm] Roscher's volumes on economics led me to develop an interest

in German Historical School economics.' But Seki stated that in the summer of 1895, when both were teaching at the Kobe Commercial School, 'Marshall's [*Elements of Economics*] was your [Fukuda's] favorite book.' It is not clear how much of Marshall's work Fukuda and Seki read in the early 1890s, but in 'Notes on readings', which Seki is believed to have written in January 1893, his third year at the Tokyo Higher Commercial School, the following note appears: 'Some notes on Marshall's *Elements of Economics of Industry*: discusses mutual benefit-ism, discusses "cooperation"' (p. 35). Seki wrote this note at practically the same time as Tatsukuro Inoue began to translate *Elements of Economics of Industry* (1892). Inoue's translation, first published in July 1896, became a bestseller; it went into a revised, eleventh printing in 1902. Marshall's *Economics of Industry* had been translated by Korekiyo Takahashi, who later became the celebrated minister of finance and the 'Keynes of Japan'.[5]

From the late 1880s to the mid-1890s Japanese economics shifted from British liberal economics, represented by Ukichi Taguchi, a sort of Japanese Manchester school, to the German Historical School and the Social Policy School. Both the Department of Economics at the Keio Gijuku School, established in 1890, and the Faculty of Law at Tokyo Imperial University came under the strong influence of the Historical School and Kathedersozialisten. This occurred at the Keio Gijuku School under Berlin University graduate Garrett Droppers, whom it invited to be head teacher when it opened, and at Tokyo Imperial University under Noboru Kanai, who entered the Faculty of Law in 1890, on returning to Japan from overseas study in Germany. It has been stated that the Russo-Japanese War was the 'springboard for historicism' and that 'upon this springboard, Japan's historical school of economics, also known as the social policy school, established itself and replaced the influence of liberalism'.[6] In 1896 the Association for the Study of Social Policy was organized with Kanai, Kakujiro Yamazaki, and Kumazo Kuwata (all from Tokyo Imperial University) as its leading figures. The next twenty-five years constituted the era of social policy as well as the initial development of Japanese economics. Economics in Japan was formed with this period as its foundation.

Teijiro Ueda, who enrolled in the Tokyo Higher Commercial School in 1896, wrote the following entry in his diary in the summer of 1899: 'The two approaches to research, the British and the German, have become the two main schools, and their various strengths and weaknesses are clear.... In economics in particular, these schools stand out; and because there are the British and German schools, Mill's liberalism and Wagner's national socialism form a duality, the two great influences' (Ueda 1965a:400–1). The entries for the decade around the turn of the century are particularly interesting, as Ueda comments on the process of the German Historical School's entry into Japan and the changes that occurred there before and after Fukuda's return. At the beginning of February 1900, he wrote, 'One

critical test is if there was great success in economics reading which I have intended since last year.' Beginning in the previous year he read Tajiri's essays on banking, Tajima's recent economic theory, Marshall's *Elements of Economics,* and J.S.Mill's *Principles*; in October 1900 he started Marshall's *Economics of Industry,* followed by the works of J.S.Nicholson, F.A.Walker, J.K.Ingram, and others. He met Fukuda in January 1902, probably for the first time, and then read Bücher beginning in March, Eugen von Philippovich and William Smart in September and October, and Philippovich again and Brentano in November (pp. 413, 419, 441, 480, 483, 492–3, 517–19).

In January to March 1903 Ueda wrote: 'with Takimoto, read Philippovich, then…read Kleinwäechter from cover to cover while doing an abridged translation…at the beginning of November, started reading Schmoller (p. 579). At the beginning of 1903, we learn, 'Since meeting Mr Fukuda I am at last starting to progress in my understanding of what the historical school is.' Later, viewing the year in retrospect, he observed: 'The center of the whole was the historical school. This [the historical school], united with the spirit, makes it clear that the law of progress is something which can also be used to operate society' (pp. 531, 579). In September and October 1903 Ueda read Schmoller and Ashley, and at the beginning of November he wrote, 'I will make research on enterprises my subject' (p. 573). Ueda later founded business economics, or management studies, in Japan.

The latter half of the Meiji period (1898–1912) was the era of the Historical and Social Policy Schools, but the economic approach which developed primarily at the Higher Commercial Schools, and the approach developed principally by Kanai at Tokyo Imperial University were significantly different. Hyoe Ohuchi (1970:35–8) observed that people like Fukuda, Seki, Sano, and Takimoto (all from the Tokyo Higher Commercial School) 'had already sat at the center of academic circles whose scope went beyond the narrow area of the commercial sciences'. In 1906, just after the Russo-Japanese War, the *Journal for National Political Economy: Economics and Commercial Studies* [Keizaigaku, shogyogaku, kokumin keizai zasshi], coedited by the Higher Commercial Schools in Tokyo and Kobe, first appeared (the first editors were Kotaro Fujimoto and Yuzo Sakanishi). Tokyo Imperial University and Kyoto Imperial University were already publishing the *Journal for State Science* [Kokka gakkai zasshi] (from 1887) and the *Journal for Legal and Economic Studies* [Horitsugaku keizaigaku naigaironso] (from 1902), respectively, but the *Journal for National Political Economy* became Japan's first real economics journal. While Kanai and his followers were proud to be the 'socialists of the chair' at Tokyo Imperial University, which was moving towards Wagnerian-style state socialism, Fukuda and his followers at the Higher Commercial Schools were sympathetic to their 'reformist liberalism' and were closer to British political economy.[7]

Marshall and Fukuda

After returning to Japan, Fukuda seems to have made economic history and economic policy his specialties. With Hajime Seki, he coauthored *Discourses on Commercial and Economic Policy* [Saikin shosei keizai ron] (1902), which was actually a translation of articles by Brentano and Schmoller. The *Principles of National Political Economy* [Kokumin keizai genron], which was published in 1903 as the first part of a general economic theory, revealed in its conception the strong influence of the German Historical School. In August 1904 Fukuda was suddenly ordered to take leave of absence from the Tokyo Higher Commercial School because of a conflict with its president. In October 1905 he began lecturing at the Keio Gijuku School, where he used Marshall's *Principles of Economics* as his textbook. From then until March 1918, he compiled commentaries on the first four books of *Principles* for his lectures and published them as *Lectures on Economics* [Keizaigaku kogi] in three volumes—the first in September 1907, the second in June 1909, and the third in September 1909. Fukuda then published them in a single volume—*Complete Lectures on Economics* [Keizaigaku kogi-zen] in September 1909.

In 1905, when Fukuda started to lecture at the Keio Gijuku School, the German translation of Marshall's *Principles* came out with Brentano's introduction. Brentano's introduction was translated and included in the first Japanese translation of the *Principles* by Kin-nosuke Otsuka. Fukuda attached a 'reviser's supplementary introduction' to Otsuka's translation, where he stated that Marshall's *Principles* were 'the pinnacle of contemporary economics, as my mentor Brentano wrote in his introduction to the German translated edition, so there was no need to attempt to add anything further'.[8]

Fukuda begins *Lectures on Economics* with the first passage from Marshall's *Principles*: 'Economics is a study of mankind in the ordinary business of life; it examines that part of individual and social action which is most closely connected with the attainment and with the use of the material requisites of wellbeing.' He then adds: 'In brief, economics is one part research on wealth while the other part is research on human beings. Therefore, the latter in comparison to the former is of vastly greater importance.' The problems of poverty and ignorance cannot be totally eradicated from human society by economics alone, but 'the greater part of the facts and reasoning necessary to resolve these problems are encompassed within the sphere of economic research, and my greatest interest in this field of study lies therein' (Fukuda 1925:1, 4–6).

As seen later in this chapter, Fukuda ultimately came to emphasize the position 'from the price struggle to the welfare struggle', but what he was also asking of Marshall was for liberation from price economics in order to build welfare economics that was responsive to the demands of the times:

> It would be the great British economist Alfred Marshall himself who should be seen as the forerunner in this trend of economic thinking outside of the German ethical school of economics. The first volume of his greatest work, *Principles of Economics,* must be seen as a great declaration of welfare economics. But with regard to the true intention of Marshall, the apostle of welfare economics, we should look at his entire academic activity rather than this work that remained as a mere declaration.[9]

In the first book of *Lectures on Economics*, Fukuda (1925:17–18) makes the following observation in comparing the British and German schools: 'Given that economists attempt to divide the structure of economics into different varieties, doing so in a general manner gives us no other than two types; the British school or orthodox school along with eclectic schools, and the German school or new historical school.' According to Fukuda, Marshall represented the former, and Schmoller the latter. British academics saw the starting point of research as investigating the activities of individuals, and they placed little importance on conceptions such as a national economy. In contrast, German scholars acknowledged the principle that economic life was regulated, limited, and constrained by a society established under the aegis of the state, and where an individual's activities are also conducted within such organizations as the family or the company, there is no sense of a totally free, unconstrained individual. Therefore he states:

> The progress of twentieth-century academics will advance a step beyond this trend of thinking. Social-based theory of the German school in the near and far future must enter the entire area, and at the same time must show another stage of advance as economics, and also as social-based and an organization-based study. However, this so far belongs to the realm of ideal, and the present reality is that in the German style of economics the struggle for a way of thinking has just concluded but the serious task of constructing is barely started. Schmoller's great life work shows that it does not go beyond borrowing of past materials and rich descriptions from all other fields; economics stops with only a small bit at the end of the second volume.... Speaking of realistic theories and of the most numerous works fulfilling the conditions demanded of academic studies, this is British economics with its individualistic view, which is not inferior to socialistic German economics.... Marshall's contention that economics is the research of the relationship between man and wealth should mean that the genuine purpose of economics could be achieved only by mastering the studies of both man and wealth. Thus, this relationship should concern not only the amount of wealth but also the possibility of providing human beings with equal material means that would be necessary to perform their higher

> developments and nobler acitivities. The new school, the historical school, the ethical school, or whatever, definitely do no more than this conception, which shows the highest, most comprehensive status in contemporary studies.
>
> (Fukuda 1925:22–5)

Fukuda criticized the German school and generally described the contemporary state of economics as follows:

> The common criticism of contemporary German scholars is that they devote themselves to policy, to the compilation of facts, and they don't emphasize the clarity of pure reason (theory). Their arguments that make up the historical narrative surprised even minutely erudite persons, but upon logical dissection they just followed or imitated many of the conventional beliefs of earlier persons, so that the original thoughts are actually rather few, and in this regard the British scholars are the best.
>
> (Fukuda 1925:132)

However, he continued, the theoretical studies of Max Weber, Werner Sombart, Franz Oppenheimer, Robert Liefmann, and Othmar Spann had suddenly become extensive. In Austria, the Austrian school had grown quite productive from the time of Carl Menger and made major contributions to theoretical economics. Above all, the works of such scholars as Böhm-Bawerk, Friedrich von Wieser, and Joseph Schumpeter could not be forgotten. Elsewhere, particularly important were P.P.Leroy-Beaulieu, Pierre Levasseur, and Charles Gide in France; Léon Walras in Switzerland; J.B.Clark, Simon Patten, and Irving Fisher in America; and in Italy, Matteo Pantaleoni, Achille Loria, and most important, Vilfredo Pareto. Other contributors included Gustav Cassel in Sweden and Karl Pearson in the Netherlands.

> The most distinguished doyen, however, was Britain's Alfred Marshall. Marshall had mastered the recent research of the German scholars, but had not neglected the purely theoretical study of the British scholars. At present, he represented the most advanced position in his discipline; at the same time, he had to be regarded as the most distinguished economist in the world. Marshall's able disciple A.C.Pigou was continuing his work, furthering his research, and becoming the leading figure among the present generation of scholars in their prime.
>
> (Fukuda 1925:133)

Further, according to Fukuda (p. 31), Marshall's ideas on welfare economy had at last been generally accepted, as was evident in the case of Britain's

most pressing political problem in 1908, the Old Age Pensions Act. The Report of the Poor Laws Commission also demonstrated that these ideas had been accepted by intelligent people. The Minority Report of the Commission, J.H.Muirhead's *By What Authority*? (1909), took on great importance. It was necessary to read this together with Sidney and Beatrice Webb's *Prevention of Destitution* (1912). One should also read Pigou's *Economics of Welfare* (1920), which further developed Marshall's concepts. Fukuda also referred to his own ideas in 'From price struggle to welfare struggle' (1921).

From price struggle to welfare struggle

Remaking economic science: social policy and statistics

The great earthquake that devastated Tokyo in 1923 afforded an opportunity to revitalize support for Fukuda's welfare economics. 'Joined with my fellow scholars I used my full ability to meet this test, on the one hand in my study, on the other in the street, to the greatest extent of my little spirit and strength, I was engaged either in meditating, or in direct engagement, in surveying, or in persuasion' (Fukuda 1924:2). The results were published in *Principles of Reconstructing Economy and Some Problems* (1924). He first discussed the principles of reconstructing economy, the welfarist meaning, and the difficulties of economic recovery at that time. In the next five sections he described surveys and proposals for dealing with the most pressing problems of the reconstruction, including unemployment and fire insurance. In the first section on 'Tokyo Before the Earthquake, Viewed by Economic Demography', he emphasized that 'economics in the future will be social policy studies with a new meaning'. He continued:

> As the social policy studies, which I call future economics, steadily develop, their sister disciplines, statistical studies as demography must enter into a greatly productive future. Many economic principles of the present day, which are no more than the techniques of arbitrary mental exercises, will certainly become laggards in the world which is sure to come. I believe that these should be replaced by the social policy science and comparative demographic statistics with a new meaning.
>
> (Fukuda 1924:366)

Fukuda applied his utmost abilities and his experience in conducting surveys on unemployment to generate economic demography, and herein lay his criticism of the price struggle. Fukuda claimed that statistics on production, prices, wages, and so on, 'stop as statistics on things, and are nothing more than something presupposing today's price economy as unchangeable'. Thus,

he believed that there needed to be 'economic statistics for humans in places where economy occurs', and conceived of an economic demography that would be 'statistical research of the living conditions of economic persons' (1924:366). The emphasis on remaking economics through social policy science and statistical studies was, as Nakayama has said, an advance in Fukuda's conception of welfare economics. Seeing economic life as a purely price-based life or a life devoted to monetary values, and nurturing a conception of welfare economics therein, was in a certain sense a policy issue. To effectively carry out the claims of welfare economics and turn it into an instrument of policy, it would be necessary to expand the research areas that depended on statistical facts (Nakayama 1930:466–7).

Fukuda strongly believed that statistical methods were of inevitable importance in economic studies. The conceptual background of his attitude towards statistical methods was, according to Nakayama, that 'he sought for the birthplace of this field of study in the Historical School'. Nakayama added:

> It is the German Historical School which has greatly contributed to the diffusion of statistical research methods in the history of contemporary economics. First, in terms of methodology, including statistical research methods, it not only opened vast new areas where empirical research should collaborate with theoretical research, but by shifting the attention of the academic world to policy and current affairs issues, either directly or indirectly, helped to diffuse statistical methods into the research methods of economics.... The credit for the basic contribution of diffusing statistical methods would clearly go to them; economic fluctuations have given rise to today's demands for statistical economics, and I believe that it is no great error to find that the framework of this structure is already visible in the opinions of the Historical School. Thus, through the twists and turns of the course of the research, Fukuda came to uphold both the empirical and realistic stances learned from the Historical School.
>
> (Nakayama 1930:461)

In February 1923 Fukuda became a member of the advisory council of the Social Bureau of the Home Ministry. He also served as head of the Imperial Economic Council's Committee on Social Housing Issues dealing with measures on temporary land and housing rentals and as special head of the Social Bureau's Central Labor Exchange Committee. In these capacities, and using the opportunity afforded by the earthquake, Fukuda, along with people like Toru Nagai, Social Bureau chairman Hiroshi Ikeda, and Toyohiko Kagawa, worked to improve the labor exchange system by drafting a bill proposing new facilities (the nationalized labor exchange).[10]

Later, an advisory council was formed by Fukuda, Izutaro Suehiro (who became the first chairman of the Central Labor Commission in 1946), and

Ginjiro Fujiwara to conduct research on wages, employment, and labor unions. On the strong recommendation of Fukuda, Nakayama, who had just returned from studying under Schumpeter in Germany, was assigned to plan and conduct surveys on unemployment as a part-time researcher. Nakayama, who had 'begun and ended with desktop meditations', later recounted that 'it was absolutely thanks to this experience of surveying unemployment that I came to have so much understanding of surveys and empirical research'. Nakayama's writings in this period indicate the connections between his and Fukuda's thought and that of the German Historical School, as well as an important continuity from Nakayama's prewar to postwar activities, when he was deeply involved in labor issues and industrial relations as the second chairman of the Central Labor Commission. After Fukuda's death, Nakayama shared responsibilities for parallel lectures on the principles of economics with Kin-nosuke Otsuka at the Tokyo University of Commerce (the new name for the Tokyo Higher Commercial School): Otsuka spoke on Marxian economics, whereas Nakayama covered so-called modern economics and published *Pure Economics* [Junsui keizaigaku] in 1933. He also produced a number of papers and articles on unemployment and unemployment statistics, and tried to develop economic sociology. In a collection written to honor the late Fukuda, Nakayama included a piece entitled 'Economic Theory and

Economic Sociology' [Keizai riron to keizai shakaigaku].[11] Nakayama, in the article 'Relations between the economic and statistical sciences for business cycle research' *(Statistical Comments,* 1932), wrote that 'the whole of the vastly significant social economics contained in economic theory is none other than the demand for a contemporary economics closely matched to an era of change'. In regard to this idea and that of a 'program of practical economies', he stated that realistic, empirical research is not necessarily the first apparent trend in

contemporary statistical studies. Not only was economics based on real experience, the instinctive foundation of the discipline, but 'In regard to the history of economics, there has already come to be reliance on the different views of the Historical School to the point that a single program has been formed.' The following quotation exemplifies Nakayama's thinking about contemporary business cycle research: 'the question of emphasis on the quantitative economics advocated by Mitchell, and of how to create the structure, for example, resemble Schmoller's economies' (Nakayama 1932:353–5).

From price economics to welfare economic studies

Fukuda's article 'From price struggle to welfare struggle: especially labor disputes as welfare struggle' appeared in 1921 in the journal *Reconstruction* [Kaizo](vol.3 no. 5:2–21), and was included in Part 2, 'Class Struggle and

Its Participants', of *Social Policy and Class Struggle* in 1922. Social policy rather than socialism, he argued, presented the best means of overcoming the defects of capitalism. The objects of both socialism and social policy, according to Fukuda, were class struggles between capitalist classes and wage-earning classes, but socialism, or at least Marxism, offered the optimistic thesis that 'holds that the fate of capitalism is that it must bring about its own inevitable collapse, and consequently must also sooner or later be vanquished'. The reason for the existence of social policy was that 'Social policy does not accept capitalism in that its inevitable fate is to bring about its own destruction.... I insist that we must trust, not to the arrival of fate, but to the policies of people, and resist this great influence' (Fukuda 1922:5–6).

Although Fukuda (1925) called Marshall 'the greatest authority among contemporary economists', he makes the following criticism in 'From price struggle to welfare struggle'. In the first edition of *Principles of Economics,* Marshall presents the clearest and boldest position of any spokesman for welfare economics, but

> starting with the second edition, he gradually follows the conventional beliefs of price economics, and at the end he falls to a lowest viewpoint —one that is absolutely no different from that of his fellows. In particular, Book V and Book VI which deal with price and distribution theory are the worst of all.... The critique that Marshall is wandering at the crossroad between the old price economics and the new welfare economics is no reckless slander.
>
> (Fukuda 1921:182–3)

The main points of Fukuda's critique of *Principles* are discernible in this statement.

'Our study of prices is not conducted for its own sake, but because we believe that it is related to economic welfare, so by studying this we hope to advance welfare research' (Fukuda 1921:189). Fukuda sought to absorb the welfare economics vision of Marshall and Pigou, but while he was strongly influenced by Pigou, his own belief was that welfare economics could not be grasped through the definitions and analysis of Pigou alone. Fukuda believed that the most important role was to deal with concrete labor issues. These included income distribution, such as whether the workers' share was equitable, whether the labor movement or labor disputes had obtained for workers a fair distribution in terms of welfare, or whether reasonable working hours were guaranteed.[12] Fukuda's welfare economics thus exceeded the neoclassical economics of Marshall and Pigou and concerned itself with policy issues, Fukuda went beyond the Cambridge School to return to the tradition of the English Historical School or the School for Social Policy, emanating from Oxford and

represented by such thinkers as J.A.Hobson, Edwin Cannan, William Beveridge, G.D.H.Cole, as well as to the economic and social policy of the British Labour Party.

> Capitalist society is an income acquisition society. What this means is that society develops by means of surplus distribution. When there is no surplus, and when there is no surplus distribution, income problems cannot exist…. J.A.Hobson's declaration that a supposed society, in which no development occurs, would have no distribution problem even now lingers in my thinking. Insofar as the position of cost principles or utility principles are concerned, the real problem of distribution does not exist in economic theory…. That is the same as the case that in the non-developing industrial society based on those principles distribution cannot exist. It must be said that Marx's clear articulation of this theory, and this one thing only, was one of the penetrating insights of the ages. It is for this reason that I place Hobson, who has not the slightest connection with Marx but who arrived at the same insight, in the first rank of contemporary British theorists.
>
> (Fukuda 1929c:163–4)

In his criticism of Pigou's welfare economics, Fukuda argued that the welfare struggle was necessary to support his theorems of welfare economics. He asserted that: it must be admitted that supposing that all of Pigou's theorems of welfare economics were true, there would be no means of implementation other than the institutions of legislative administration and self-governance for social policy. But the *raison* d'*etre* of social legislation, social administration, social self-governance, and social policy must be found exactly in the realization of three qualifications to his first theorem [increase in national income promotes economic welfare]. Only labor movement aimed at welfare struggle can be a countermeasure against [1] compulsion of labor against the will and interest of workers, [2] worsening of income distribution, and [3] variability of national income. Other institutions are weak and useless; insofar as they work, they are based on and supported by labor movement as welfare struggle (Fukuda 1921:203–5)

Fukuda's tentative conclusion was the development of communal principles for capitalist society, which he stated in 'Production, exchange, and distribution of surplus: the development of communal principles in capitalist societies' (*Reconstruction,* vol. 11, no. 7, July 1929). The communal principles of 'from each according to his ability' and 'to each according to his need' are 'woven into the texture of contemporary capitalist society, like the thread of fate, through the whole of production, exchange, and distribution'. These principles appear not in price theory but only in income theory, and cannot be found in the conflict between cost principle and utility principle. 'When we realize the existence of the surplus principle and see the flow of the surplus directly, the principles will loom…albeit

dimly.' 'In capitalist society, the "struggle for surplus value" develops, step by step, through class struggle, through "labour contract", through "minimum or subsistence wage", through workers' insurance or unemployment insurance, and, further, through the taxes of the capitalist state and the public authorities, and through the various public corporations and the public institutions' (Fukuda 1929c:178–9).

Fukuda believed that the development of communal principles would be found in the progress of capitalist society or in the stage of the 'highly developed capitalism' *à la* Werner Sombart, but admitted at the same time the tentative advance of communal principles in the progress of the British welfare state. On 10 June 1929, immediately after the establishment of the second Labour Government in Britain, Fukuda wrote:

> I learned from this morning's newspaper that Mr MacDonald, in his installation ceremony speech on the evening of the 8th, stated that the major tasks of his new cabinet would be to reform the industrial system and solve the unemployment problem. The formation of this cabinet may be as much as a major 'development of communal principles' in Britain, and I think it may largely affect the future of British capitalism, by which my interest has been deepened to a new degree.
>
> (Fukuda 1929c:183)

Then, in 'The inevitability or not of unemployment and the possibility or not of an unemployment policy' (*Reconstruction, vol. 9 no. 9,* September 1929), he stated:

> In this chaotic arena, I admit that the correct principle has raised its head like the thread of fate. I see this as a further example of 'the development of communal principles in the capitalist society'. Most of all, I acknowledge its remarkable development among the people in the Labour Party who have formed Britain's new cabinet. How this cabinet will go forward and what kind of things it will do in the future cannot be foreseen at present. However, the plan of 'Economic General Staff appeals to my attention. I find *The Next Ten Years in the British Social and Economic Policy* by the former guild socialist Cole as the powerful basis. This work will probably be brought out as the intellectual ledger for the new cabinet.
>
> (Fukuda 1929b:215–16)

Postscript

From the 1860s, as English classical economics rapidly waned, the Historical School and the Social Policy School came to occupy the leading positions in economic thought. The German Historical School in particular

spread outside Germany and exerted a powerful influence. There are important areas for investigation on the international diffusion and transformation of the Historical and Social Policy Schools during this era, particularly in Britain, where the Classical School tradition was entrenched, and in Japan, where no such tradition had existed. This chapter is a step in that direction. Marshall, who first traversed the path from labor problems to economics, bestowed high praise on the German Historical School and held many points in common with it. But, Marshall, who optimistically believed in 'the possibility of a vast improvement in the condition of the working classes' through a market economy (Marshall 1890:763), parted ways from the Oxford Economists as well as the English Social Policy School and founded the solid basis of neoclassical economics. In the course of the institutionalization of Marshall's economics, his thought, which was comparable to the German Historical School, seems to have been almost forgotton.

Even though praising Marshall highly, Fukuda criticized price economics and worked to develop the Historical School aspects of Marshall's thought regarding 'the social policy study as the economics of the future'. Although attracted to both Marshall and Pigou, Fukuda criticized price economics and wholeheartedly advocated a labor movement and labor struggle in the form of struggle for welfare and human rights in order to go beyond price struggle—Fukuda termed this 'welfarization'. To investigate the standpoints of Marshall and Fukuda on labor problems in the historical context of Britain and Japan, and to compare the vision of Marshall, who emphasized educational investment and human capital along with organic economic growth, with that of Fukuda, who stressed human rights, welfare economy, and labor struggle, would be an interesting subject. Fukuda's argument on labor issues emphasized 'human rights' and 'welfarization', and he indicated differences from Marshall with regard to the introduction of Taylorism.

Notes

1 Brentano's writings were entitled *Über das Verhältniss von Arbeitslohn und Arbeitszeit zur Arbeitsleistung* (1876). Quotation from Sakanishi (1933).
2 Brentano is quoted from Brentano and Fukuda (1899:2359–60).
3 Nakayama (1978:64–7).
4 Ueda (1930; 1921:3). Hitotsubashi University (1950:118). Fukuda (1960:6–7).
5 Fukuda left the Kobe Commercial School to enter the newly created graduate program [Kenkyuka] in the Tokyo Commercial School in 1895; he submitted his dissertation, 'Commercial Crisis and Depression of Trade', in 1896. Hajime Seki, 'Notes on Readings', MSS, in Hajime Seki Papers, Editorial Office of the History of Osaka. On Inoue and Marshall, see Inoue and Sakaguchi (1993: 220).
6 Ohuchi (1949:3–4).
7 Hitotsubashi University (1950:362–3). Ohuchi (1949:52) wrote that the Social Policy School 'could be called the "first-class stage" of Japanese economics in that era, and the research reports and public lectures of this group during a two-

day conference provided an exhibition of the efforts and achievements of Japanese economists of the era; speaking with a little pride, I believe that it can be said that Japan's historical economics and social policy school begin and end with this collection of work.'

8 Otsuka (1919); Hayasaka (1972).
9 Fukuda (1921; 1922:182–3).
10 Fukuda (1924, 2nd introduction). On the advisory council of the Social Bureau of the Home Office, see especially *History of the Home Office* [Naimusho shi], vol. 3 (Tokyo: Chiho Zaimu Kyokai, 1971), p. 396.
11 See Nakayama (1933:79–100; 1972).
12 See Yamada (1965:456) and Nakayama (1978:70–1).

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Chapter 11

The impact of German economic thought on Japanese economists before World War II

Osamu Yanagisawa

In the 1920s and 1930s the historical development of capitalism and its transition from free competition to an organized economy was discussed extensively in Germany, where the historical method of economics was much more influential than in any other European country. Even before World War I, German economists began to speak of the rise of big enterprises in heavy industry, their organization in cartels, and the growing influence of banks on industry. The new and 'late' stage of capitalism, bringing a decline in competition, the growing importance of monopoly, the organization of the economy, the state's intervention in the economy, and the decay of the capitalist spirit were debated by Marxian intellectuals and non-Marxian scholars alike. After World War I the structural change in capitalism was one of the most contested topics in the Verein für Sozialpolitik.[1] In the conferences of the Verein in 1926, 1928, and 1932, not only scholars of the German Historical School but also social democratic intellectuals such as Emil Lederer and Rudolf Hilferding and young liberal economists like Walter Eucken and Wilhelm Röpke argued about the features of the contemporary changing capitalism in historical perspective, in which the 'late' capitalism asserted by Werner Sombart became one of the most prominent topics.

The German observations about changing capitalism and discussions on the present stage of capitalistic development as well as its future prospects attracted the attention of contemporary Japanese intellectuals. In Japan, where German economic thought, especially of the Historical School, had prevailed since the 1880s,[2] the German analysis of the changing process of capitalism from free competition to an organized economy and of doctrine for the government's future regulation of the economy was helpful to an understanding of the present stage of Japanese capitalism and the problems of economic control by the government, which were accelerated by the depression of the 1920s and 1930s, and especially by the expanding military operation in China. This chapter deals with the influence of German economic thought about the issues of changing capitalism and its future reform on Japanese discussions of organized capitalism and state control of the economy before World War II.

Beginning of the organized economy in prewar Japan

In the history of social science in prewar Japan, the so-called 'debate on Japanese capitalism', which began in the 1920s and continued in the 1930s, marked an important turning point in the study of economics. The participants in the controversy, most of whom were professors at universities and scholars of the social and economic theory of Marxism, discussed the historical development and special features of capitalism in Japan, which retained the remnants of feudalism in its social and economic structure.[3] But the political repression under the growing militarism in Japan, which prevented the growth of liberalism and democracy in the country, brought the debate to a close by 1936–8, when prominent participants in these discussions were arrested or forced out of the universities and henceforth silenced.

In addition to this well-known controversy involving Japanese Marxism, which had enduring significance for the progress of the social sciences in the postwar era, another series of arguments arose with the development of capitalism in Japan before World War II. The views of the parties to this dispute were mostly based on non-Marxian doctrines, often influenced by the social and economic thought of contemporary Germany including national socialism. They concerned the present stage of capitalistic development, the problems caused by the decline of free competition and organization of the economy through cartelization, and the importance of reform of the economic system through government control of the national economy, as Shirakizawa (1988, 1999) observed. To confront the difficult social and economic problems caused by the depression, the Japanese government at that time established measures to control the economy. The Important Industries Regulation Act [Juyo-Sangyo Tosei Ho], implemented in 1931 and revised five years later, was important to the discussion on the organized economy in Japan. The government's regulation of the economy was accelerated by Japanese military expansionism in Asia, especially the war against China (1936), which required that the national economy be organized for a state of war. The issues disputed in discussions on the organized economy mirrored the economic and political realities confronting Japan in the 1930s, and the argument was inevitably connected with and influenced by actual state policy. Although the debate among Marxist intellectuals was forced to a close under the growing militarism and political suppression, the controversy surrounding the new organized capitalism continued and was even extended, as state control of the economy escalated with the expanding war. Indeed, the concrete, technical problems of controlling the economy to promote the war effort were increasingly deliberated with the expansion of the war into the Pacific war.

As Kichihiko Taniguchi (1935), professor at the University of Kyoto, wrote: there were two approaches to the study of the organized economy:

(1) analysis of the development of the organized economy in the present stage of capitalism (the *Sein* approach), and (2) exploration of future reform of state regulation of economic activities (the *Sollen* approach). Both these approaches could lead to various reforms in the present regulation of the economy, ranging from a *laissez-faire* policy to eliminate state intervention to the comprehensive organization of the economy by the state.

Sombart's Die *Zukunft des Kapitalismus* in prewar Japan

In 1933 and 1934 the new ten-volume work, *Regulation of the Economy in Japan,*[4] made a significant contribution to the prevailing discussion of organized capitalism and state regulation of the economy. After that many books and articles on these topics were published in Japan until the end of the war in 1945. Various concepts on the development of capitalism emerging from contemporary Germany furnished the bases for understanding this subject at home, although Japanese intellectuals often referred to Anglo-Saxon economists like John Maynard Keynes, George D.H.Cole, Lewis Lorwin, and John Maurice Clark as well. According to Japanese publications, especially helpful were the works of Christian Eckert, Friedrich von Gottl-Ottlilienfeld, Carl Landauer, Emil Lederer, Oswald Lehnich, Ludwig von Mises, Heinz Müllensiefen, Fritz Naphtali, Friedrich Pollock, Walther Rathenau, Eugen Schmalenbach, Werner Sombart, Othmar Spann, Adolf Weber, and Max Weber. Among these, however, Sombart's *Die Zukunft des Kapitalismus* (1932) was among the most important regarding the 'late' stage of capitalism. The ideas in this small book were accepted by many Japanese scholars, as they provided various insights into the problems of present-day capitalism in Japan. A prominent professor of economic history, Sombart had been well known in prewar Japan, where his work *Luxus und Kapitalismus* had been translated into Japanese in 1925. The Japanese translation of *Die Zukunft des Kapitalismus* appeared in 1933, only a year after its publication in Germany, and Sombart's *Die drei Nationalökonomien* was translated into Japanese in the same year. Some of his other works, such as *Der Krieg und Kapitalismus, Die Juden und das Wirtschaftsleben, Deutscher Sozialismus,* and chapters of *Der moderne Kapitalismus* were translated several years later.

In *Die Zukunft des Kapitalismus,* in which he summarized his lecture on 'Wandlung des Kapitalismus', presented at the conference of Verein für Sozialpolitik in Zurich in 1928, he considered the structural changes in the capitalistic economic system from three perspectives—namely, its modification of the economic viewpoint, its order, and its technique. With respect to the change in economic viewpoint, he argued that the capitalistic spirit, unique to capitalism, showed a considerable transformation within those decades. According to Sombart, the capitalistic spirit, which was caught between rationalism and irrationalism, between speculation and

calculation, between citizen mind and robber spirit, between reflection and venturing, became reduced as rational considerations increased considerably and a rationalizing spirit made itself felt even among the formerly speculative capitalists. He asserted that information for economic activity could be acquired more easily and the manager of the enterprise tended to build it on a scientific system, so that the business became like an administration of government and its managers received the status of officials. At the same time, striving for profits diminished in favor of safety and stability; the inclination to take risks and the desire for adventure began to decline; as a result of concentration, price cartels, the incorporated enterprise, etc., financial powers connected with industries became greater.

The order in the economic system of capitalism, so argued Sombart, itself changed: liberalism and individualism in the economy, as legal, moral and conventional, diminished and became more restrained. This was produced by (1) the self-restriction among individual businessmen through bureaucratizing and regulating their firms and by means of cartels, (2) regulation by the state, the protection of workers, by the arbitration process and price control, and by direct supervision, and (3) the regulation by trade unions—appointing the staff in firms, regulating tariffs, and the like.

For Sombart, the changes in the process of economic life were the most important. He pointed out that the market mechanism with its automatic process, on which the capitalistic system rested, had been eliminated: supply and demand no longer determined the condition of the market, which had formerly decided the price of commodities, wages, and profits. On the contrary, now prices were fixed arbitrarily by the cartels and wages were fixed by trade unions, so that prices and wages remained at the previous level. Sombart wrote

> These changes which the economic system of capitalism has experienced in an extensive as well as an intensive respect, are noticeable on all sides, and have caused me to speak of a new epoch into which economic life has entered, and which I have characterized as the epoch of late capitalism, according to my systematic scheme of economic epoch.
>
> (Sombart 1932:11)

Besides the changes in the national economy, the structure of the world economy changed substantially after World War I. Sombart contended that the world economy in the age of 'high capitalism' [Hochkapitalismus] had been based on free trade on the gold standard and on a regulated exchange of foreign currency among the capitalistic countries, which was essentially managed by the City of London. At the same time European capital had been invested, either directly or through public loans, in non-European countries, and Western Europe absorbed the natural products of countries

worldwide, which purchased industrial products from Europe. Those assumptions, on which the world economy before World War I was based, could no longer be maintained after the war, as a number of those countries that were industrialized came out of these relationships. Pointing to the prevailing customs barriers, import prohibitions, recall of credits, and the failure of the gold standard, Sombart asserted that the mechanism of free trade had collapsed. And, with the industrialization of formerly agricultural countries, the international exchange of goods between Western Europe and those countries, which was characteristic of the nineteenth century, would cease: the absorbability of those nations with respect to industrial production would diminish, the industrial exports of Western Europe would fade away; and the system of exploitation exercised over 'colored races' by Western Europe, the 'domination of the white race' on earth, was definitively at an end. Out of those considerations he concluded that nations leaned toward self-sufficiency—i.e. there was a tendency toward autarky, in which small countries would unite into economic blocs, having a sufficiently wide basis to build an economic system, be, to some extent, self-contained. With regard to the future, Sombart saw three possibilities: maintaining the status quo (conservative), turning back to a free economy (reactionary), or building up a well-planned, systematized economy (reformative-revolutionary).

The planned economy that Sombart envisioned should be extended to production, circulation, distribution, and consumption—therefore to all branches of economic life. The planning must not be a system of restrictions in all cases; rather, there should be enough zones of freedom, especially in consumption, within which everyone could do just as they pleased. He affirmed at the same time that planning must be carried out from one central administration. And the planned economy must always be a national economy, in which self-determination would be only partly restricted.

One characteristic of the planned economy, Sombart observed, would be the diversity of economic life; it was madness to try and formulate one uniform plan for all economic conditions. He affirmed that one must consider the size of economic districts, as well as the difference in the social structure of a country, the character and culture of its people, and its history. Opposing the adoption of a monistic economic form planned by 'Utopiants', such as 'Sovietism', Sombart argued that a multifarious economic life required different means of formulation, and the more complicated the economic life, the more its apparatus must be extended. Thus the planned economy, according to Sombart, should provide for the coexistence and interlocking of many varied economic forms and devices, so, for example, there would be a private, individualistic economy and a market economy, as well as collective 'demand-meeting' economy in the same planned economy.[5]

The influence of Sombart's *Die Zukunft des Kapitalismus* in Japan was far-reaching. In *Principles of the Regulated Economy,* the first book of the previously mentioned ten-volume work on the regulated economy in Japan, Shikamatsu Mukai, its author, describes Sombart's book in detail and appraises his ideas (Mukai 1933:217–22, 238–42). Mukai's book, as an introduction to and a standard work on the regulated economy, contributed to the expansion of Sombart's argument of 'late' capitalism. Sombart was also esteemed in Yoshio Hon-iden's volume, *Theory of the Controlled Economy* (1938:5, 26–7), and in Kaname Akamatsu's *Regulation of the Industrial Economy* (1937). Both books were read widely and had a profound effect on the discussion of the controlled economy in prewar Japan.

The influence of von Mises, Schmalenbach, and Rathenau on the views of Mukai and Hon-iden

Shikamatsu Mukai and Yoshio Hon-iden were among the prominent economists engaged in the discussion of the organized economy in prewar Japan. Mukai, a professor at University of Keio, left academe during the war and occupied positions in the Chamber of Commerce and Industry in Nagoya and in the Central Committee of Cooperation of Commerce and Industry. Hon-iden, who had been an influential professor of economics at Tokyo University, resigned his academic post and, like Mukai, devoted himself to making policy for the control of the national economy during World War II. Both men thus contributed not only to the discussion on the issues, but also to actual policymaking for the wartime economy.

In *Principles of the Regulated Economy,* Mukai (1933:230–8) argued that, with the division of labor within the enterprise and society, the national economy would inevitably move from a market economy with free competition to a regulated and then a planned economy. He regarded the present development of scientific management in the United States on one side and the rationalization movement in Germany on the other as typical for such a process. With technical progress industries would be organized step by step and competition would be limited, then abolished. As for transition to the planned economy, he outlined five stages: (1) the age of the market economy with free competition, (2) the age of monopoly capitalism, i.e. privately regulated economy, in which the market economy was limited, (3) the age of the regulated economy with the beginning of intervention and control by the state, (4) the early planned economy [partielle Planwirtschaft], in which important industries were managed by the official power structure (greatly limiting the market economy), and (5) a perfectly planned economy without a market. He pointed out that the nineteenth century was the age of economic liberalism and the twentieth century began the regulated economy.

Mukai's argument relied mainly on the discussions in contemporary Germany. His vision of Japan's inevitable transformation to a regulated economy was drawn from Werner Sombart as well as Eugen Schmalenbach. Mukai, whose field of economics was management and enterprise, especially depended on Schmalenbach's article 'Die Betriebswirtschaftslehre an der Schwelle der neuen Wirtschaftsverfassung' (1928). Mukai argues that, according to Schmalenbach, the existence of monopolies in cartels and trusts, state enterprise, price controls, regulation of house-rent, and foreign exchange controls, which prevailed in the advanced countries, signified a transition from a liberal economy in nineteenth century to a regulated economy [gebundene Wirtschaft] in the twentieth century. This transition was rooted in the increasing economic power of large enterprises with a growing proportion of fixed cost to commodity value, which produced the monopolies, for example, in cartels.

Accepting the opinion of Sombart and Schmalenbach on the development of capitalism, Mukai and Hon-iden concluded that a reasonable future system would be a partly organized economy, somewhere between socialism and *laissez-faire* capitalism. On the other hand, they regarded socialism (perfect planning of the economy without money) as difficult and inhuman, paying special attention to the criticism of Ludwig von Mises, who had believed that a socialist system of planning, which lacked a market price system based on private ownership, could not work. Mukai (1933:276–86) summarized von Mises's *Kritik des Interventionismus* (1929), which attracted many contemporary Japanese intellectuals.[6] According to von Mises, there were various types of government intervention in the economy in which price control would play a special role. Thus government could fix the price to be less than the level that would be decided in a free market system, but there would be a shortage of commodities because producers and merchants would not sell their goods at such a low price (instead, reserving them in their stores). Then the government would be forced to extend a control to the prohibition of such a practice, the use of a quota system, or the fixing of the prices of raw materials and wage rates. Moreover, the state's regulation of price would not be limited to a few important industries, but must include all industrial sectors and thus cover all prices of commodities and all wages. Mukai and Hon-iden agreed with this theoretical consideration of von Mises, but could not accept his argument that the existing economic depression was caused by state intervention, which created monopolies, and that only the abolition of government control and a return to *laissez-faire* liberalism could solve the present economic difficulties. They emphasized that the market mechanism was no longer workable and self-controlled as in the age of liberalism, and criticized Mises for neglecting the fact of a decline of the liberal economy. Mukai and Hon-iden believed that neither socialism nor a return to *laissez-*

faire capitalism could be useful in the future and affirmed that only through government regulation of the economy could Japan resolve its problems.

For Mukai's image of future economic reform, Walther Rathenau's notion of 'Autonome Wirtschaft' was especially important. Mukai, in his previous work *Management Economics* (1929), had dealt with the development of management and enterprise and expressed great regard for Rathenau's observation concerning the division between the management and ownership of stock in corporate enterprise, and the increasing independence of the former from the latter in modern times. The concept of 'autonomous' enterprise, which Rathenau asserted in his publication *Autonome Wirtschaft* in 1919, is examined in detail by Mukai in his *Principles of the Regulated Economy.* Rathenau argued that the age of a free market economy had ended and that the economic system must be organized and managed successfully with the aid of state planning, but not through the 'socialization' [Sozialisierung] or 'nationalization' [Verstaatlichung] of enterprises. Private enterprise would continue and professional elite managers would play an important role, but no longer for the sake of profit, which had created various economic and social problems, but for the welfare of the society. Based on Rathenau's *Autonome Wirtschaft,* Mukai affirmed the expectation that such an autonomous enterprise (supercorporation in his words), which was neither capitalistic nor socialistic, could assume a leading role in the partly regulated and organized economy of the future. From this point of view Mukai criticized the closed and monopolized ownership of stocks of the Zaibatsu concern in prewar Japan, as it had disturbed the development of small and medium-sized firms and blocked innovative economic activities. He demonstrated that opening the stocks and shares of the Zaibatsu to the public was necessary to create the new economic system.

The abuses of monopolies were also denounced by Hon-iden. The increasing power of monopolies, he observed, such as cartels and trusts, to determine the prices of commodities damaged the role of capitalism that had previously served public objectives through the competitive and productive activities of enterprises. In fact, the present economic difficulties were recognized by the monopolistic enterprises themselves; they were now forced to seek the organization of the national economy to get out of the depression. Hon-iden expected that in the future the Japanese economy would be regulated through the extension and organization of cartels and enterprises on one side and the control of their economic activities by the government for the public good on the other. In considering the organization of the national economy, however, Hon-iden believed that self-regulation of the organized enterprises was more important than direct control by the state. It is likely that Rathenau's view on the organization of the economy through the transformation of cartels into public bodies controlled by the state influenced Hon-iden, though he made no special reference to it in his book.

The views on the organized economy and expectations for its regulation by the government that prevailed among Japanese intellectuals were criticized by Tsunao Inomata and Itsuro Sakisaka, who were main participants in the Marxian debate on Japanese capitalism. In his contribution to the ten-volume work on the regulation of the economy, Inomata (1934) surveyed, from the Marxian viewpoint, the contemporary thought and policy of economic regulation, such as the views of H.S.Person, Hugo von Hahn, Lewis Lorwin and Gerard Swope, and policies of the New Industrial Recovery Act in the United States and of national socialism in Germany, compared with and contrasted to socialist planning in Soviet Russia. Sakisaka (1934), whose analysis, like Inomata's, was based on Marxian theory, investigated the various doctrines of the regulation in the United States, Germany, and Japan, and praised the writings of Carl Landauer (*Planwirtschaft und Verkehrswirtschaft,* 1931), Emil Lederer (*Planwirtschaft,* 1932), and Friedrich Pollock ('Die gegenwärtige Lage des Kapitalismus und die Aussichten einer planwirtschaftlichen Neuordnung', 1932), which were critical of the prevailing thought on economic planning. Inomata and Sakisaka agreed that capitalistic depression could not be surmounted by a partly regulated economy, which would only strengthen the power of monopolies and cartels.

Cartel problems in the organization of industry

In the debate on the organization of industry in prewar Japan, there were three principal issues: (1) the rise of large enterprises, the monopolies in cartels, trusts and combines and their control by the state, (2) the organization of small and medium-sized firms, and (3) the development of public corporations managed by the state or municipalities. These topics related to actual economic and social problems at that time, and the views of Japanese intellectuals often reflected their personal attitude toward Japanese policy at the time of the economic depression and the military expansion in Asia, which forced the nation to strengthen and organize industry for war. Among the three issues mentioned above, the control of giant corporations and monopolies by the government and the problems of small businesses were of the most concern, and attempts to resolve them drew on German economic doctrine to the greatest degree.

Hiromi Arisawa's *The Regulation of Industries in Japan,* published in 1937, contributed much to an understanding of the problems. Arisawa, who was arrested in 1938 for promulgating a method of economic analysis based on Marxian theory and was forced to give up his professorship at the University of Tokyo, had already examined the development of monopolies in capitalistic countries (Arisawa 1931) and provided an analysis of the mobilization in Europe and the United States during World War I (Arisawa 1934). In *The Regulation of Industries in Japan,* Arisawa investigated the

structure of Japanese industries and government policy to regulate them. He concluded that Japanese industries were divided into two groups: (1) a number of large enterprises in basic industries that were to be regulated by the Important Industries Regulation Act of 1931, and (2) vast numbers of small and medium-sized firms in various branches, especially consumer goods industries, that were to be organized in trade associations. Arisawa, like Mukai and Hon-iden, held that in the 1930s regulation of the economy was a general tendency in the capitalistic countries, to which Japan also belonged. He focused on the cartelization of enterprises, their amalgamation with the state, and their transformation into public bodies, through which economic regulation by the government was put into practice.

To understand these developments, Arisawa (1937:215–64) surveyed the views of economists on the problems of cartelization in Germany— among them, Friedrich Kleinwächter, Theodor Vogelstein, Max Metzner, Gustav Schmoller, Emil Kirdorf, Siegfried Tschierschky, Heinz Müllensiefen, Herbert von Beckerath, Oswald Lehnich, Arnold Wolfers, Hans Stark, Robert Liefmann, Walther Rathenau, Carl Landauer, Rudolf Hilferding, and Georg Halm. Arisawa paid special attention to the debate on cartels between Schmoller and Kirdorf in the 1905 conference of the Verein für Sozialpolitik in Mannheim.[7] Schmoller had regarded the cartel as a product of the development from small businesses to large enterprises, from the free competition of many small and medium-sized firms to the centralized direction and monopolies of organized large enterprises, and from *laissez-faire* to social and state organization of national labor. Cartels, though they had helped to lessen the effect of economic depression, had misused their power in the market, raising artificially the prices of the commodities they produced. Foreseeing that industrial monopolies would become powerful enough to eclipse the state, Schmoller recommended that a cartel act be drafted to observe and control the activities of cartels. In defense of cartels, Kirdorf, the general director of the Gelsenkirchen Mining Corporation, argued that the private monopoly, as a child born out of economic difficulties, was a necessary product. He asserted that cartels, whose ability to decide market prices had been overestimated, would not misuse their power, as they could not continue to exist if they did so. Thus, unlike Schmoller, Kirdorf opposed the regulation of cartels.

In postwar Germany, where cartels again became the subject of controversy, the decree against the misuse of economic powers was implemented in 1923. With respect to the effect of this decree, Arisawa took note of the view of Müllensiefen and Wolfram Dörinkel:[8] cartel regulation was effective, not in the case of large enterprises, but only for small and medium-sized firms, whose economic power was weak.

At the same time Arisawa did not overlook the new interpretations of cartelization in Germany, as expressed in the writings of Beckerath and Lehnich who were sympathetic to cartels, regarding the changing character

of cartels:[9] a cartel, as a product of economic difficulties produced by destructive competition, gives order to the competitive market and regulates the production and sale of commodities in a reasonable fashion. With cartels, according to them, competition can exist in various forms to prevent such monopolies from raising prices merely to increase profits. At the same time, Arisawa noticed that some German economists who were critical of cartels, such as Carl Landauer, Kurt Wiedenfeld, Hans Stark, and Siegfried Tschierschky, argued that cartels were forced to consider the interests of 'border' firms which would raise prices above the level that would be determined under free competition. Arisawa himself contended that cartels would aim to eliminate outsiders and to cease competitive struggle among the members of cartels, which could be solved, however, not by themselves, but only with the help of the state, such as a decree to limit capital investment; cartels and the state would thus be consolidated.

Concerning the combination of cartels and the state under National Socialism in contemporary Germany, Arisawa had great regard for the opinion of Carl Landauer expressed in 1923.[10] Citing Landauer's fear that the prevailing cartels would be most dangerous to democracy, Arisawa pointed out that democracy had indeed ended under National Socialism in Germany, where cartels, as public bodies for the organization and control of the market economy, were given an important role in the new economic system of the Nazis.

In Japan, discussion on problems associated with cartels focused on the government's industrial policy at that time, in which the Important Industries Regulation Act of 1931 had a special significance for the organization of the principal industries during the depression. The Act had aimed to protect and support the cartels of enterprises through government in order to abolish unreasonable, destructive competition among them and to create stability and order in the economy. At the same time the government could regulate cartels, if necessary, through the Act, with a decree that the state should control the activities of cartels and prevent the misuse of monopolistic power. The heated debates that occurred in political and business arenas, when the act was revised in 1936, stimulated discussion among intellectuals on the problems of organized capitalism as well as the regulation of the economy. In those debates it was important to understand the development of cartels and their control by the government in light of events in Germany. As Hideaki Miyajima (1988) observed, the prominent officials in the Ministry of Commerce and Industry who had prepared the Regulation Act and applied it in practice, such as Nobusuke Kishi, had learned much from developments in Germany, and their views were strongly influenced by contemporary German thought on cartels, like that of Oswald Lehnich, who saw in the combination of enterprises a production promotion function.

The actual problems of the Important Industries Regulation Act and its revision also became a topic debated by intellectuals. In his writings Arisawa (1934, 1937) analyzed this Act and drew attention to problems that it would create. Keizo Fujita in his book *Struggle over Cartels* (1936), in which he assessed the doctrine of Fritz Kestner and Oswald Lehnich (*Organizationszwang,* 1927), tied his criticism of cartels to the act that was being revised. He regarded the Act as a cartel regulation law in Japan. Many books and articles concerning the organization of enterprises were published after that. As the title of the book *Regulation of the Economy and Cartels and Trade Associations* (1939) indicates, its author, Kazuto Kunihiro, considered the role of economic combinations to be managing groups in the organized system of the national economy, especially of the compulsory cartels and their regulation by the government. His work also relied on German economic doctrines.

Toward World War II

With the beginning of the war against China, Japan shifted to a wartime economy. Both the government and the military endeavored to increase the productive capacity of the munitions industry and to organize and control the national economy (Hara 1998). The discussion of economic issues broadend and became more concrete and realistic, especially so after the onset of the Pacific war. At that point the government considered the regulation of almost all economic activities including consumption, as well as the control of every economic institution. The 'regulation of the economy' became a byword among Japanese intellectuals, especially economists. The regulation of the economy was increasingly understood in connection with the wartime economy, an economy organized for total war. The problems of the regulated economy were thus considered frequently as a topic of a technical method of economic mobilization for war; it was assumed that control of the economy would cease when the war ended.

Many Japanese intellectuals, however, pursued the regulation of the economy that would continue to establish a new economic order after the war. They envisioned that postwar Japan would enter a new stage of economic development, in which the self-interested activities of individuals seeking high profits that had created problems such as monopolies would be controlled and the economy would be reformed for the welfare of society. Those views were often colored ideologically by militarism and social conservatism that supported and justified the present war. Implicit in this way of thinking was a criticism of economic liberalism, which was related to political antiliberalism and anti-democracy, as well as to a skepticism of classical economic theories and the doctrine of '*homo oeconomicus*' in economic thought. A number of scholars, inspired by the social conservative viewpoint, made an effort to mold the traditional

economic thought inherited from ancient Japan, based on Tennoism, into a 'Japanese economies'. Haruki Naniwada's five-volume *State and Economy* [Kokka to Keizai], published in 1938–43, was a product of those attempts. Naniwada, who had translated Werner Sombart's *Deutsche Sozialismus* into Japanese in 1934, was an influential professor of economics at Tokyo University, but was compelled to leave the university when the war ended.

In the context of the conservative tendency in academe in Japan, contemporary German doctrines, which prevailed in Nazi Germany, attracted the special attention of some Japanese economists. Friedrich von Gottl-Ottlilienfeld was one of the leading figures in this direction. *Der Weg der deutschen Volkswirtschaftslehre,* edited by Erwin Wiskemann and Heinz Lütke, translated into Japanese in 1943, demonstrated a conservative interpretation of the German Historical School. At the same time, however, a number of scholars criticized, though not explicitly but with careful restraint, the ideological interpretation of economic thought and the political atmosphere in academe in wartime Japan. Some of them devoted themselves to the study of social science in a truly academic manner. In the field of German economic thought, such investigations dug deeper into the works of Friedrich List and Max Weber. The results of the exploration during this difficult period, especially that of Hisao Otsuka, Kazuo Okochi, and Zenya Takashima, created a basis for the subsequent development of the social sciences in Japan.

Notes

1 *Schriften des Vereins für Sozialpolitik,* vols 172, 175, 187. See also Yanagisawa (1998) and Brandt (1993:397–402).
2 Hoston (1994, pt 3). See also Fujii (1998).
3 See Ando (1998).
4 Mukai (1933, vol. 1); Ryu (1934, vol. 2); Kawai (1933, vol. 3); Itoh (1933, vol. 4); Takahashi (1933, vol. 5); Arisawa (1934, vol. 6); Hijikata (1933, vol. 7); Kojima (1933, vol. 8); Inomata (1934, vol. 9); Sakisaka (1934, vol. 10).
5 Cf. Backhaus (1996), especially the article by Günther Chaloupek.
6 See also Hon-iden (1938:29–30, 37–9).
7 *Schriften des Vereins für Sozialpolitik,* vol. 116, Leipzig, 1906, 376–438.
8 Arisawa was referring to the conclusions drawn by Müllensiefen and Dörinkel in their work, *Das neue Kartell-, Zwangskartell-, und Preisüberwachungsrecht* (1933).
9 See Herbert von Beckerath, 'Der Inhaltwandel der Kartellbegriff und seine wirtschaftlichen Folgen', *Wirtschaftsdienst* 12, no. 30 (1926), and Oswald Lehnich, *Kartell und Staat* (1928).
10 See Carl Landauer, 'Die Wege zur Eroberung des demokratischen Staates durch die Wirtschaftsleiter', in *Erinnerungsausgabe für Max Weber,* vol. 1 (München/Leipzig, 1923).

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Chapter 12

Walter Eucken and Wilhelm Röpke

A reappraisal of their economic thought and the policy of ordoliberalism

Naoshi Yamawaki

Strictly speaking, the ordoliberalism represented by Walter Eucken and Wilhelm Röpke does not belong to the German Historical School. On the contrary, both economists began to develop their theories in opposition to the Historical School.[1] Nevertheless, their economic thought and policy did adopt several positive aspects of the School. It is therefore important to be clear about which features of the School ordoliberalism accepted and which ones it rejected, whether explicitly or implicitly. It is also important to evaluate the significance of ordoliberalism in view of its influence and its potential. Starting from this concern, the first two parts of this chapter characterize the economic thought and policy of Eucken and Röpke and the last part considers their significance in postwar Germany as well as for the present time.

Eucken's economic theory and policy

Walter Eucken (1891–1950) began his career as an economist in the 1920s at the University of Bonn under the guidance of Joachim Schumacher and Heinrich Dietzel, who evidently opposed the German Historical School. Having lost such strong leaders as Gustav von Schmoller and Lujo Brentano, the Historical School of those days could not deal with the economic crisis in the Weimar Republic. In particular, the hyperinflation of the early 1920s convinced Eucken of the fundamental weakness of the Historical School, which was incapable of taking any measures against such unprecedented, disastrous inflation. To make matters worse, the school's approval of the monopoly or cartel encouraged the National Socialism of the Nazi Party, which assumed power in 1933. To counter the objectionable aspects of the German Historical School, Eucken, as a professor of economics at the University of Freiburg, put forward a new theory. Naturally, his new theory was ignored under the Nazi regime and did not come into its own until after World War II.

Two major works of Eucken, whose thought exercised great influence on the postwar economic policy of West Germany, were *Die Grundlagen*

der Nationalökonomie (1940) and *Grundsätze der Wirtschaftspolitik* (1952). These two volumes present Eucken's original position on the economy, as distinct from any other theory of economics.

Economic theory as epistemology of economic order (ordo)

At the start it should be pointed out that Eucken regarded his new theory not as value-neutral but as value-laden. In this sense, his economics was rooted in his philosophical thought, which confronted not only the German Historical School but also various other economic theories. According to Eucken, the greatest mistake of the Historical School lay in its presupposition of the stage theory of historical development based on a belief in social progress. The Historical School, as represented by Friedrich List, Karl Knies, Wilhelm Roscher, Bruno Hildebrand, Karl Bücher, Gustav von Schmoller, etc., assumed, in spite of its nuances, that the stage of historical development would correspond to the degree of progress of a given society. But this assumption was theoretically inadequate and practically misleading.

Theoretically speaking, many historical facts of the past refute the validity of the historical stage theory as an index of social progress. For example, the economic institutions and productivity of the ancient world reached their zenith in the third and second centuries BC and declined during the Roman Empire. In fact, the historical events in this long era show just the opposite of Hildebrand's notion of development from a 'natural economy' via a 'monetary economy' to a 'credit economy'. In the third century BC in Egypt, a 'credit economy' flourished and decayed in the course of the following centuries. The Roman banking system as a 'monetary economy' prospered in the second and first centuries BC and disappeared under the Empire. Moreover, in the third century the barter economy came to be regarded once again as a 'natural economy'. Similarly, real historical process refutes Bücher's scheme too, because the Hellenistic states in the third century BC had already reached the stage of a 'national economy' and then regressed to a 'household economy' in the long process of history. Thus, the real economic development in history shows not only social progress but also social regression (Eucken 1992:69–90).

Practically speaking, such a progressivistic stage theory is not in a position to deal with the challenges of social realities that never can be deduced from it. World War I overturned Schmoller's optimistic view of social policy based on his belief in the harmonious ethico-economical development that would lead to social progress. The inability to take measures against hyperinflation in the 1920s revealed that the stage theory did not adapt well to the situation. The emergence of Nazism was nothing but a regression of society and then the stage theory played a tragic role to support it. Moreover, it was evident that Marxian economics, captured by another kind of stage

theory called historical materialism, had been playing a disastrous role in suppressing the spontaneous actions of the people in the Soviet Union (Eucken 1992:223–73).

In this way, Eucken rejected the stage theory of historical development as an index of progress. Since not only social progress but also social regression could be found throughout world history, it was important for him to understand economic realities from a different viewpoint. And for this purpose he introduced as his key concept economic 'order' [ordo]. Ordo, he declared, would permit an understanding of the economic reality at any period in time:

> Whether it is the economy of the ancient world or of Augustan Rome or of medieval France or modern Germany or anywhere else, every economic plan or economic action of every peasant, landlord, trader, or craftsman takes place within the framework of economic order, and is only to be understood within this framework. The economic process goes on always and everywhere within the framework of historically given economic order. The order may be a bad one, but without order no economy is possible.
>
> (Eucken 1992:80)

The task of the economist is to acquire a knowledge of the structure of actual economic orders that either grew spontaneously or were created legally.[2] In his view, however, there are generally only two types of economic order: (1) the 'centrally directed economy', in which the control of the entire economic life of the community follows the plan of a central authority, and (2) the 'exchange economy', in which two or more independent economic plans are formulated and carried out. Within these two types, several variations are to be found, and Eucken calls the method to gain this kind of knowledge 'morphology'. Morphology makes it an important task for economists to find economic order in a given socioeconomic reality. To be sure, the real economic world shows an unlimited multiformity. But the morphological discovery of the elemental forms of which present and past economic orders are composed makes it easy to grasp and understand the multiformity (Eucken 1992: part 3).

As far as the organization of the market is concerned, Eucken gives five forms of supply as well as demand: competition, partial oligopoly, oligopoly, partial monopoly and monopoly. The combination of these forms of supply and demand characterizes the forms of the market such as perfect competition, partial oligopoly of supply or demand, bilateral partial oligopoly, and partial monopoly of demand (supply) limited by partial oligopoly of supply (demand). The morphological method, which analyses and understands a given economic reality in this way, is quite different from the economic theory of the German Historical School, which could not appreciate the market economy (Eucken 1992:156–8).

Yet at the same time Eucken's economic theory, so far as it always understands the real economic world from both a theoretical and a historical perspective, is distinct from pure theoretical economics, which disregards the historical situation. One must keep in mind that a given economic reality is a historically changeable object. Accordingly, its morphology has not only a static but also a dynamic character and always considers such non-economic data as legal or political order. For Eucken, economic theory as the epistemology of the economic order cannot be separated from historical reality, and therefore the dualistic division of labor between economic theory and economic history, into which the Austrian School derived from Carl Menger seems to have fallen as well, is unsupportable. In other words, the economic theory gets its relevance just by being able to grasp historically generated concrete realities. The abstract models called 'pure economies' in particular make no sense, so long as they have nothing to do with historical reality (Eucken 1992:295–317). It is clear that Eucken adopted this positive feature of the German Historical School, though he rejected any stage theoretical approaches by which it had been captured.

Economic policy in light of a well-ordered society

The most influential aspect of Eucken's economics, however, was his position on the economic policy. Just because of this position, his economic thought became known as 'ordoliberalism'. Against any positivistic view that regards a theory as value-free, Eucken asserted that a good or better economic order can be distinguished from a bad one and the bad one must be replaced by the good one. Economic policy must therefore aim at criticizing a bad economic order as well as bringing a good or better one into existence. The criterion for distinguishing the good from the bad is whether a given economic order is compatible with the freedom of human action, because the concept of order (ordo) is ultimately to be connected with the freedom of a human being as a personal order. In Eucken's view, Kant's idea of enlightenment, which in the late eighteenth century attached much importance to the freedom of individuals from any authority, has been frustrated since the nineteenth century, especially in the economic area. This occurred with the emergence of new economic powers like cartels, Konzern (concerns), large trade unions and pressure groups that deprived workers of their freedom. The workers were forced to subordinate themselves to these new powers. To solve this social problem, Eucken advocated not socialism but a new liberalism. He argued that socialism is unable to understand the merits of free competition and the market order, which promotes the free activities of individuals, and instead endorses a centrally planned economy. Eucken regarded such a socialistic idea as totally wrong. The labor unions movement, he believed, also has a dangerous

aspect in that it subordinates the freedom of the workers as individuals to the collective decision-making organization. This is why he stood against socialism and for economic liberalism (Eucken 1952: ch. 11).

The economic liberalism that Eucken supported was also different from *laissez-faire* liberalism such as that of the Manchester School. The economic liberalism originally advanced by Adam Smith in the late eighteenth century intended to promote the spontaneous activities of individuals that would produce unexpected public benefits under the guidance of the invisible hand of God. But, in fact, this thought could not achieve its goal. The realities of industrialized society since the nineteenth century betrayed not only Kant's philosophical liberalism but also Smith's economic liberalism. In Eucken's view, the most serious mistake of the nineteenth-century *laissez-faire* liberalism, such as that of the Manchester School, was that it failed to understand the importance of an adequate relationship between the market as a well-ordered economy and the state as a political agency. The market as a well-ordered economy cannot be realized without an 'order policy' implemented by the state (government).

For a well-ordered economy, the main role of the state is not to hinder free competition, but to prevent the formation of economic powers like cartels, trusts, and monopolistic capitalists so as to maintain free competition among the economic agencies. Paradoxically, the *laissez-faire* liberalism, which sees the state merely as the enemy of a free economy, unintentionally contributes to the formation of economic powers that suppress free competition (Eucken 1952: ch. 4). From such insight it follows that Eucken's liberalism attaches much more importance to the state than did other concepts of economic liberalism. Though Eucken and Austrian neoliberals like Ludwig von Mises and Friedrich von Hayek shared a distrust of the centrally planned economy, they differed on the role of the state.[3] Whereas Austrian neoliberals denied that state intervention in the market could have any positive result, Eucken believed that free competition could be guaranteed not spontaneously but by an 'order policy' decreed by the state. For this reason, the concept of 'spontaneous order' later advocated by Hayek may not have been acceptable to Eucken. Moreover, their attitudes towards social policy differed as well. Whereas the Austrian neo-liberals regarded social justice generally as the route to any kind of socialism,[4] Eucken accepted this idea, as long as social justice improved living standards without impairing free competition. Since the worker must be respected as a person rather than treated as a means to maximize profits, the promotion of cooperation between employers and employees as well as the social policies by the state did not conflict with Eucken's view of liberalism (Eucken 1952: ch. 18). Consequently, his notion of 'market economy' came to be regarded as 'social market economy', as Alfred Müller-Armack coined the term.[5]

Eucken's economic thought thus shows us another kind of liberalism. What ultimately characterizes Eucken's liberalism is the concept of 'ordo' (order), which is not confined to the economic order but comprehends the importance of the legal, political, and personal order as well. This is why it is called 'ordoliberalism'. Indeed, 'ordoliberal' is just another name for those who aspire to a 'well-ordered society'. Ordoliberalism is concerned not merely with economic phenomena but with other social problems from the comprehensive standpoint of ordo, although it is aware of its limits as economic thought. For Eucken, the most important aim of the modern social sciences was to investigate a given historical reality in light of ordo and to determine which ordo would be the most appropriate for an industrial society (Eucken 1952: ch. 19). Based on its historical perspective, his liberalism took up the positive legacy of the German Historical School without falling into the stage theory.

Röpke's humanistic society and economy

The other influential ordoliberalist is William Röpke (1899–1966). After leaving Nazi Germany and teaching at Istanbul, Röpke moved to Geneva and there published his major work *Civitas Humana* (1944). While living in Geneva, he had a marked influence on economic thought and policy in West Germany after the war as well as liberal-conservative intellectuals throughout the world. Because his thought was wide-ranging, to reflect modern civilization itself, it may be called 'social thought' rather than 'economic thought'. Unlike Eucken, Röpke did not criticize the German Historical School explicitly, but his opposition to modern social progressivism as well as the stage theory is fundamental to his thought. In confronting the social crisis of his time, he tried to rehabilitate economic society with a human face and called his attempt the 'Third Way'.[6]

A Third Way against collectivism and capitalism

What Röpke called the 'Third Way' was simply a means to replace both collectivism and capitalism, which had been causing a profound crisis in modern civilization. According to him, in human society there are only three types of economic order: the 'self-contained economy', the 'market economy' and the 'coercive economy'. The self-contained economy' in its purest form is one that solves problems within a self-sufficient, undifferentiated economy of the peasant family producing of its own account. Feudalism may be regarded as its degenerate form. The market economy in its purest form comprises genuine competition, and the monopoly is considered its degenerate form. The coercive economy is nothing more than a collectivist command economy, one that is necessarily illiberal and anti-democratic, as typically seen in Nazi Germany and the

Soviet Union. Vindicating liberal and democratic values in a cultural sense, Röpke insists that only the market economy in its non-degenerate form is compatible with liberal-democratic values rooted in humanity (Röpke 1996:1–40). A genuine market economy should not, however, be confused with capitalism, as he describes it:

> 'Capitalism' is the distorted and soiled form which market economy assumed in the economic history of the last hundred years. Genuine market economy and a competitive structure are just what capitalism has not been at any rate for the past fifty years, and this has been the case to an ever greater and disturbing extent.
>
> (Röpke 1996:27)

With such a negative view of capitalism, Röpke emphasizes that a genuine market economy is just the opposite of monopoly and business concentration and of that anarchy of pressure groups that had been spreading in all countries. Consequently, what he calls a 'Third Way' to overcome the modern social crisis must be a way to replace both collectivism and capitalism. And, evidently, this way is closely related to Eucken's economic thought.

Unlike *laissez-faire* liberalism and like Eucken's ordoliberalism, Röpke is of the opinion that a market economy cannot function automatically and therefore requires the help of the state. He considers a satisfactory market economy to be less a spontaneous order than an artistic construction and an artifice of civilization, which has this in common with political democracy. Röpke stresses the need for a positive economic policy that consists of 'framework policy' and 'liberal interventionism' as an important task of the Third Way. Framework policy tries to create good frames in which a market economy can function well. Liberal interventionism means intervention by the state into a market economy not to adjust it but to reserve it.

To these two policies must be added what Röpke calls 'structural policy'. This policy deals with the social conditions of the market economy such as the distribution of income and property, the size of businesses, the distribution of population between town and country as well as between industry and agriculture, and class distinctions. But it does not regard these conditions merely as facts but as objects to be changed. It is just this idea of structural policy that characterizes Röpke's economic thought most strongly. Against monopolies, concentrations of businesses, and mammoth capitalism, this policy works on behalf of small and medium-sized business in every branch of economic life. Against the proletarianization of the people, it strives for deproletarianization by re-establishing property for the greatest number (Röpke 1996:28–31).

But these three economic policies, though they make the market function well, do not suffice for Röpke's Third Way. According to him, the market

represents only one narrow sphere of social life. In other words, human beings are not merely economic beings such as competitors, producers, businessmen, union members, shareholders, savers, and investors, but also social beings as members of their families, neighborhoods, churches, and communities. Furthermore, each individual has his or her own sentiments, passions, and ideals. This is why Röpke's Third Way does not confine itself to the politico-economic level but goes on to the level of anthroposociological framework to be considered. He describes the anthroposociological task of the Third Way as follows: 'The social and humanitarian principle in the frame must balance the principle of individualism in the core of the market economy if both are to exist in our modern society and at the same time the deadly dangers of mass civilizations and proletarianization are to be avoided' (Röpke 1996:32). Thus Röpke's Third Way is not merely liberal but also comprehensive social thought that includes concrete economic policies as a vital prescription in the face of modern collectivism and capitalism. In this sense, he may be called a social philosopher rather than a socioeconomist.

Social philosophy for a humanistic society

To be sure, *Civitas Humana* can be regarded as a socio-philosophical book, especially as it addresses the moral foundation of society. For Röpke, it is unacceptable to engage in social science without regard to value judgment. Since human beings are the most important agencies in society, social science cannot do without value judgment. So far as social facts are mediated by the human consciousness, they must be judged in terms of values. Otherwise, the moral relativism that makes human actions blind as well as nihilistic would become dominant in the name of science.

From such a perspective, the first target of criticism was Saint-Simonism, an influential modern view of social science and society born in early nineteenth-century France. According to Röpke, Saint-Simonism is characterized by 'the attitude of mind which is the outcome of a mixture of the hubris of the natural scientist and engineer mentality of those,…who would construct and organize economics, the state and society according to supposedly scientific laws and blueprints' (Röpke 1996:63). It is just this view that forms the ideological backbone of social engineering planned by the national elite not only in France but also in other industrial countries. Eliminating the human element from social science and, instead, idealizing the organization, planning, rationalization and functionalization of society, this view leads to collectivism as an enemy of human society. Social theory based on a humanitarian value judgment has to stand against such a unilateral and anti-humanistic, but also very influential ideology (Röpke 1996:61–79).

Röpke's social philosophy also makes a distinction between a healthy government and a sick government. In short, the healthy government has three elements: legitimacy, association, and decentralization. In particular, the element of decentralization is all the more important because many governments since the French Revolution have become more and more centralized and sick (Röpke 1996:85–96). To endorse the merit of political decentralization for a healthy government, Röpke refers to the 'Principle of Subsidiarity' in Catholic social doctrine; this means that 'from the individual upward to the central government the original right lies with the lower rank and each higher rank only subsidiarily takes the place of the rank immediately below it if a task is beyond the capacity of the latter' (Röpke 1996:90). This liberal as well as hierarchical principle limits the authority of the central government and protects the rights and the liberty of the lower ranks. In contrast, the modern centralized government has been tending towards bureaucratization for the planned economy and for exploitations to satisfy the desires of elite parties or pressure groups.

In addition to this sickness of modern government, Röpke pointed out the 'congestion' (Vermassung) and 'proletarianization' of society as a pathological phenomenon of modern Western civilization (Röpke 1996: 131–64). Mass society has been destroying human communities and depriving each individual of a sense of responsibility. Accordingly, people's lives have become increasingly atomistic and rootless. The atomized individual is no longer capable of taking responsibility in human communities—families, schools, churches, workplaces, etc. —and instead tends to subordinate himself to anonymous authorities such as mass communication, advertising, and the like. Proletarianization, which resulted from rapid industrialization, is another, less conscious pathological process of modern society. In Röpke's view, it is wrong to perceive this problem simply as a matter of the material standards of life that can be solved by higher wages and shorter working hours. The thrust of this issue lies in every destruction of an independent existence no matter how low the standard of living may be. In other words, the proletarianization is merely a large-scale change from a qualitative independent life to a quantitative, mechanical, and uniform life. Unfortunately, the Beveridge Plan for the realization of the welfare state, proposed in Great Britain, is also based on this wrong idea. A social policy like the Beveridge Plan, rather than solving the issue of proletarianization in this sense, would instead promote the bureaucratization and centralization of the state (Röpke 1996:142–51).

Then what should be done to overcome this pathological phenomenon? Röpke's reply to this question was, first of all, to decentralize big cities and industries. The decentralization of large cities inhabited by masses of people would create real communities and the conditions for a more natural existence. That was the major purpose of town and country planning based on solid anthropo-sociological foundations. The decentralization of

industries would make it possible for the greatest number of people to enjoy an independent and fulfilling life. Another important task is to strengthen the peasant core of the national economy. Of course, this would entail confronting all kinds of agrarian collectivism and thus require a sound market economy (Röpke 1996:169–95).

What, finally, can be said about an international economy in light of Röpke's social philosophy? To begin with, the idea of a world state must be abandoned because it would create collectivist political systems under which the market economy could no longer function. Second, the bloc economy has to be rejected as a collectivist (coercive) form, whereas the world economy is recommended as the international market economy. Third, to rehabilitate the world economy on a sound basis, there should be various agreements among nations pledging, for example, to renounce new international war indebtedness, to return to moderate tariff policies, to limit national sovereignty, to develop a general political order for all nations, and to establish an international currency system. Röpke's diagnosis and prescription applied to the present as well as the future (Röpke 1996:224–35).

In this way, his social philosophy was indeed very wide-ranging and comprehensive. Although he lived in Geneva after the war, his thought became influential as a significant variation of ordoliberalism in West Germany.

The significance of the thought of Eucken and Röpke

The influence of ordoliberalism on the postwar German economy: neither Keynesianism nor laissez-faire *liberalism*

It was neither Keynesianism nor Austrian neoliberalism but the ordoliberalism of Walter Eucken and Wilhelm Röpke together with other theorists like Alexander Rüstow and Alfred Müller-Armack that played a socio-philosophically decisive role in achieving the economic miracle in the Federal Republic of Germany after World War II. The key concept which stood for the influence of ordoliberalism in West Germany was the 'social market economy' alien to both Keynesianism and Austrian neoliberalism.[7]

What distinguished the social market economy from the Keynesian notion of a 'mixed economy' were Eucken's and Röpke's view of the relationship between the market and the state. For Ordoliberals, the government intervened in the market to ensure free competition and to avoid the formation of economic powers such as oligopoly or a monopoly, whereas for Keynesians, the government intervened in the market primarily to achieve full employment without regard to what economic order would result from that action. Accordingly, the tendency towards a centralized economy mattered little to Keynesians, whereas for Ordoliberals it was to

be seriously avoided. Since the spontaneous and innovative actions of private enterprise play an important role in the promotion of productivity and economic development, the government must not restrict free market competition but support it as a matter of 'order policy'. From this standpoint, centralization of the economy in the name of the welfare state is regarded rather as an evil than as a good. This is why the Federal Republic of Germany calls itself a 'social state' instead of a 'welfare state'.

This characteristic of the postwar German economy endorsed by ordoliberalism is all the more conspicuous when compared with the rapid economic growth in postwar Japan. The most influential economic thought in Japan in the 1960s was Keynesianism. During that decade, government intervention in the market in the name of financial investment [zaisei tohyushi] was supported and justified by many Japanese Keynesians. Ironically, the country's centralized economy since the prewar era, far from becoming decentralized, remained strong at that time. The term 'administrative guidance' [gyosei shido] for industries used by the bureaucracy in referring to its control of industry, which Ordoliberals would not accept, was regarded favorably long after the postwar era had ended. This is one of the reasons why the legacy of the so-called 1940s economic systems is discussed among Japanese scholars to this day.

As far as ordoliberalism was concerned, Japanese scholars barely knew what it was and sometimes confused it with the *laissez-faire* liberalism of the Chicago School, represented by Milton Friedman. For, unlike in prewar Japan, where the German Historical School had a considerable influence in academe, most Japanese economists in the postwar era usually advocated one of two approaches: (1) dogmatic Marxian economics [marukei] based on the stage theory, or (2) the so-called modern economics [kinkei] imported from the United States. It seemed to Japanese scholars as if the German approach to economics had vanished with the fall of the Historical School.[8]

Ordoliberalism differed, however, not only from Keynesianism but also from *laissez-faire* liberalism such as that advanced by the Chicago School. Both Eucken and Röpke believed in the merits of the market, but they did not believe that it could function automatically without the help of the government. In this sense, government was not seen as an enemy but as a friend of the market, and the libertarian economics of today's world would not have been acceptable to Ordoliberals. Moreover, the fundamental attitude of Ordoliberals towards workers was different from that of *laissez-faire* neoliberals. Whereas neoliberals, who emphasized the importance of efficiency, paid little attention to the circumstances of workers and even regarded the trade (labor) union as unnecessary, the Ordoliberals, who intended to establish a harmonious relationship between efficiency and social justice, took the situation of workers seriously and attached much importance to union-management cooperation [Mitbestimmung]. This is why they added the adjective 'social' to 'market economy', which Austrian

neoliberals like Hayek (1988) rejected. It can be said that in this regard ordoliberalism adopted the positive aspects of the German Historical School without accepting its inclination towards a planned economy.

It was just such original thinking that offered a strong basis for the economic policy implemented by Ludwig Erhard, West Germany's economic minister during the years 1949–63. Nevertheless, the influence of ordoliberalism declined in the 1960s and was all but forgotten as a conservative ideology in the Adenauer era, especially after the Social Democratic Party (SPD) rose to power in the 1970s.

Re-evaluation of the ethico-historical thinking of Eucken and Röpke

Though ordoliberalism declined, the legacy of the social market economy has remained in Germany. This is evident from the fact that neither Thatcherism nor Reaganomics—endorsed by neoliberals in Britain and the United States—was ever adopted, even by the conservative Christian Democratic Union (CDU) government in the 1980s. The 'order policy' as well as union-management cooperation, both features of the social market economy, continue in Germany. And the disorder in the 1990s after the collapse of the socialist planned economy seems once again to have emphasized the significance of ordoliberalism in three ways. First, the shift from a socialist planned economy to a market economy requires an appropriate 'order policy'.[9] Second, the idea of 'Rhine capitalism', as distinguished from Anglo-American capitalism by Michel Albert (1991), renewed the merits of the social market economy. Third, even among social philosophers in the English-speaking world, the idea of a social market economy began to be appreciated, as John Gray (1993) explicitly shows.

Under these favorable circumstances, it would be worth briefly reevaluating the original thought of Eucken and Röpke from a socio-philosophical viewpoint. Indeed, they were clearly aware of their ethical and historical way of thinking. It makes no sense for them to conceive of an economic order without considering its ethico-historical dimension.

What relevance does their ethico-historical thinking have to the present time? In my view, their ethical thought should first be re-evaluated in terms of the methodology of economics. Today's mainstream economics, represented by the neoclassical perspective, deals with the ethical dimension of economy merely from the viewpoint of efficiency. Neo-Austrian liberalism, which stands against a mechanical explanation of the economy, as shown in the neoclassical equilibrium theory, shares with neoclassical economics this ethical negligence. In contrast, Eucken emphasized that the justification of the economic order must ultimately be based on the personal order. In this sense, his epistemology of the economic order has fundamentally ethical traits. The market economy does not exist for its own sake, but for the sake of individual freedom. This ethical justification of

the market economy seems to be reinforced by Röpke, whose idea of 'Civitas Humana' is nothing but a socio-ethical criticism of anti-humanistic collectivism, capitalism and scientism. At the same time, the strength of their ethics lies in its combination with real policies. Their socio-ethical thinking was not unrelated to its feasibility, but always took it into consideration. Their ethics was not utopian as was that of neo-Austrian liberalism, but realistic and far more practical than neoclassical economics. Therefore, in today's academic environment, where neoclassical economics and neoliberal economics had been dominant, their ordoliberalism could offer an alternative methodology of economics based on humanistic as well as realistic socio-ethics.

This realistic aspect of their ethics was closely related to their historical thinking. Though Eucken rejected the stage theory of development presupposed in the German Historical School, he never thought that the economic order could be really comprehensible without regard to its historical reality. The morphology advocated by his analysis grasps and understands a given economic order in a given historical situation, a method that has merit in avoiding both the progressive view of history and a historical economics. For Eucken, economic development does not always accompany social progress. On the contrary, it has often caused social regression, too. Such historical thinking, which was alien to the Historical School, is relevant today when we consider the negative effects of economic development on the environment. Eucken's historical approach could offer a non-progressive as well as pluralistic view of this increasingly significant issue. In this sense, the relationship between the 'economic order' and the 'ecological order' would be one of the most interesting themes to be considered in a renewal of ordoliberalism.

Röpke's humanistic social philosophy, which rejected progressivism as well, had strongly ecological traits. His historical thinking intended not to detect social progress, but to recover the decentralized, ecological human society destroyed by modern collectivism and scientism. After the collapse of communism, his thought indeed offered a vision of the economy with a human face and accordingly a critical viewpoint on the future of the European Union (EU). For Röpke, who recognized the limits of national sovereignty, the EU's gravitation towards a centralized economy led by the bureaucracy would have been an evil to be absolutely avoided, and he would have called for the EU's unequivocal adoption of the principle of subsidiarity. Thus, in considering the orientation of the EU, he would have remained a social critic with a humanitarian outlook.

Notes

1 On the careers of Eucken and Röpke, see Nicholls (1994).
2 I regard the translation of the German word 'Ordnung' into the English word 'system' as inadequate and therefore use the word 'order' in this text instead.

3 On the Austrian neoliberals, see von Mises (1949).
4 See Hayek (1976).
5 On Müller-Armack, see Makoto Tezuka's chapter (13) in this book.
6 Of course, a Third Way in Röpke's sense is quite different from the recent Third Way advocated by Giddens (1998) as an attempt to renew social democracy.
7 On the history of the 'social market economy', see Nicholls (1994).
8 It would be desirable to study the merits and demerits of the ordoliberal paradigm in economics in view of its relevance to the present Japanese situation.
9 On this theme, see Koslowski and Chen (1996).

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Chapter 13

The economic reconstruction plan of Alfred Müller-Armack

What is the Social Market Economy?

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The German economy, i.e. the economy of the Federal Republic of Germany developed after World War II, is called a 'Social Market Economy'. On what theory, if any, is this kind of economy based? Was it formed under any particular circumstances? It is not easy to answer these questions, because it is difficult to define the Social Market Economy in terms of economic theory. Alfred Müller-Armack used this term first in a debate about the reconstruction of the German economy. But before it was appropriated by economists, the term came to be used widely by politicians and journalists.[1] A Social Market Economy was incorporated in the platform of the Christian Democratic Union (CDU), which became the ruling party of the Federal Republic. In time, the economic policies of Cabinet Minister Ludwig Erhart came to be associated with the term, which was used widely during the rapid economic reconstruction of Germany produced by the so-called 'economical miracle' in the 1950s and 1960s. Not only did Müller-Armack coin the phrase 'Social Market Economy' but also, as one of Erhart's most prominent advisers, he was deeply concerned with contemporary economic policy. Therefore, his thoughts on the subject must be considered in order to understand the implications of the Social Market Economy.

Yet the concept of the Social Market Economy was not Müller-Armack's alone. At present, the concept most associated with the Social Market Economy is probably 'ordoliberalism', an ideology of the Freiburg School represented by Walter Eucken, Professor of Economics, and his colleagues in Freiburg. In the early 1940s the school was already secretly discussing the problem of economic reconstruction after the war. The basic principles of the Social Market Economy were a product of these discussions. Müller-Armack cannot be called a member of the Freiburg School, although he is counted as an Ordoliberal, because he was in Münster and moved to Cologne in 1950. But many ideas suggested by the Ordoliberals were synthesized by Müller-Armack to form the basis of the Social Market Economy. Therefore, the understanding of the Social Market Economy varies from one Ordoliberal to another; it is never the same and the arguments

presented by Müller-Armack do not always represent the model of the Social Market Economy. He can be considered exceptional among the ordoliberals if it can be demonstrated that the German Historical School influenced his views.[2]

Ordoliberalism

The tides of neoliberalism flowed into Western Europe in the early twentieth century. One of them was ordoliberalism. It originated in the 1920s and 1930s as a reaction against the increased state restriction of human freedom. In about 1920 Ludwig von Mises, Professor of Economics in Vienna, began to emphasize the principle of the 'spread of control' to warn of the danger of such restrictions.[3] Walter Eucken, Wilhelm Röpke, Alexander Rüstow, and others followed him. Their misgivings became reality with the rise of National Socialism and the establishment of the central control system, and Röpke and Röstow went into voluntary exile. Although Eucken and most members of the Freiburg School did not rebel openly against the National Socialists, they did not accept Nazi ideology and secretly contemplated a post-Nazi economy. When the war ended they gathered around Eucken and in 1948 started the *Ordo* bulletin.[4]

The philosophical core of ordoliberalism is 'order theory', promoted in 1940 by Eucken in his book *Die Grundlagen der Nationalökonomie*. It is said that the market economy as a competitive order is fully supported by his argument, which we will now examine in detail (Eucken 1989).

The competitive order is protected on the basis of two principles: the 'principle of the Ordo' and the 'principle of the interdependence of orders'. The Ordo is the ideal order which corresponds to both the attributes of humans and of things. If 'freedom' and 'nature' are each attributes, the Ordo is, as it were, the condition of 'natural freedom'. It is a competitive order if it is limited to the economic sphere. Therefore, the realization of the Ordo should be the ultimate goal for mankind. Although the economic sphere is distinguished from other spheres, it is unrealistic to think that the competitive order can be achieved if freedom is permitted only in the economy. Conversely, if control and direction are widespread in the economy, man cannot expect perfect freedom in other spheres of life. So far as we want freedom, we must make the economy follow the principle of freedom for a whole society.

Insofar as ordoliberalism chooses the market economy as a competitive order monistically, it seems that this assertion is fairly similar to the position of classical liberalism. But the way in which the two doctrines regard the actual condition of the competitive order is fundamentally different. The Classical Liberalists contended that if government ceased to interfere in the economic process, the competitive order would happen automatically. The Ordoliberals were less optimistic than the Classical Liberalists, although they

believed that freedom was most important in a market economy. Rather, they considered the formation of economic monopoly, the aggravation of a social crisis, the appearance of a dictator, and so on, to be the result of *laissez-faire*. For them, the competitive order was the ideal order. This is why they attached great importance to making the actual economic order approach the ideal as much as possible and asked the state to establish the legal and institutional framework for that purpose.

Obviously, ordoliberalism is very ethical, because it considers freedom as the ultimate value. All things must be made to correspond to freedom. The idea that freedom itself is denied is not admitted by anyone. On this point, ordoliberalism is probably perfect liberalism. But as far as the importance of power control (i.e. the Leviathan) is acknowledged, it is sometimes called 'authoritarian liberalism'.[5] These characteristics of ordoliberalism originate in the way of thinking where the 'social crisis' must arise without compulsory rules. Alan Peacock and Hans Willgerodt (1989:5), who translated the basic treatises of ordoliberalism into English, tried to interpret such authoritarianism in the context of modern German history. Germany has been both a perpetrator and a victim of barbarism in the twentieth century, and it may be thought that this provides enough evidence to support the claim that social crises do occur without rules.

The biggest concern for Ordoliberals is how the value of freedom should be protected. From the perspective of economics also, the issue of freedom takes priority. In other words, ordoliberalism treats economics as a moral science. It is well known that Max Weber (1904) criticized the ethical character of the German Historical School and asked that value judgments be excluded from social science. It seems that the Ordoliberals rejected his request, but this was not necessarily so. Weber's intention was not to deny the meaning of value in science. Rather, he was conscious that value was critical for science. Therefore, he could not accept the fact that the economists of the German Historical School made value-judgments unconsciously. Under these circumstances, he considered how the objectivity of such recognition could be ensured if social science must be based on a subjective value-judgment. As for the historical conditions under which Ordoliberals began their activities, a value-judgment was decisive beyond the age of Weber. Therefore, they had to advance their research while being fully conscious of their own value-judgment. But it is said that their viewpoint met what Weber required.

The origins of the Social Market Economy

Müller-Armack began to argue for a Social Market Economy in the aftermath of defeat. His 1966 book *Wirtschaftsordnung und Wirtschaftspolitik* contains his writings of the postwar period. In the preface

he tells us: 'Since it was felt necessary to find a new basis for reconstruction by the end of the war, I changed my study object from religious and cultural sociology to practical economic problems, and grappled with the concept of the Social Market Economy first by the various articles right after the war, and then by my book *Wirtschaftslenkung und Marktwirtschaft* published in December 1946' (Müller-Armack 1966:10; my translation). He announced his proposals for economic reconstruction in one journal after the other after the end of the war,[6] and presented the formula for a Social Market Economy in his 1946 book.[7] He was probably able to introduce his plan so early because he had already developed the prototype during the war.

Wirtschaftslenkung und Marktwirtschaft consists of two parts: the first is an examination of economic control and the second of the Social Market Economy. A draft of the first treatise was almost complete by May 1944 (Nicholls 1994:120). Of course, this draft was subsequently refined. But it does show that the critical aspects of the Social Market Economy had occurred to him in wartime.

The aim of the first part is to prove that control is not admirable by demonstrating the actual reality of control. Although his foundation is the analysis of the economic policy of National Socialism during World War II, his purpose is 'to discover, beyond such an independent case, the destiny which is common to all economic control' (Müller-Armack 1966:20). In other words, he offers a fundamental criticism of the ideology of economic control. His reasoning is as follows. The ideology of economic control was accepted universally after the worldwide economic panic in 1929, and thereafter there was a natural tendency to reject the principle of the market economy. Accordingly, 'the perfect image of the economic planning of centralization has been drawn, and the method of adjustment to the market economy has been excluded from Germany's economic policy, especially since 1933' (p. 21). From the scholar's perspective, experience must be generalized if the various principles of economic control are examined historically. Such a judgment was the premiss of his work. Therefore, he emphasized the importance of the comparison between the reality of the market economy and the reality of economic control. 'The reality of the market economy must not be contrasted with the ideal of economic control. As for the evaluation of economic control, the expectation which the people had for control must not be made the basis of judgment. Because it was actually a problem of how many promises were fulfilled' (pp. 21–2).

Clearly his strong discrediting of the economic management of the Nazis was at the back of his mind. It has been said that the problem of German reconstruction after 'the Third Empire' collapsed was also on his mind. But he was careful about expressing his views under the actual rule of National Socialism. Müller-Armack developed the argument that the problem was connected directly to the 'choice of the economic order' (p. 21). What kind

of economic order should be made the basis of Germany's future? Should it be economic control or a market economy? An 'examination of economic control' was conducted on a preliminary basis to answer these questions. With this work he could expose the various defects of economic control and also show the original meaning of the market economy.

The second part was written after the war. German reconstruction is really the main subject, although even here the author maintains that the issue is one of choosing the appropriate economic order. The damage inflicted during the war was severe, and economic reconstruction must be expedited. Under such conditions Müller-Armack asks: 'What method will achieve German reconstruction most promptly?' (p. 78). Germany is pressed for a fundamental decision: i.e. whether to select a controlled economy or a market economy. In his opinion, a meaningful realistic policy can be formulated once the choice has been made about economic order. A reconstruction policy is meaningful when it is consciously related to economic order. In other words, a concrete policy for economic reconstruction must be guided by the choice of economic order.

It has been said that Müller-Armack's proposal was very political. The starting point of his argument is the fact that the necessity of choosing an economic order is not at all appreciated, for the defects of economic control have not yet reached 'public consciousness'. Moreover, he is fully conscious that economic reconstruction justifies increased control (p. 80). His aim is to stem this flow by raising the choice of economic order. The implications of his plan have a wider meaning when one considers that Germany was then governed by the occupation forces who promoted economic control. It was natural that his assertions were soon received by the political party (CDU) established in accordance with the move towards German reconstruction.

For Müller-Armack, a market economy was the only alternative to economic control by National Socialism during the war. Therefore, the market economy was never examined in and of itself. But the situation changed completely when 'the Third Empire' collapsed. Müller-Armack recognized that reconstruction of the market economy was inseparable from 'German reconstruction', i.e. the 'conquest of the occupied system' was urgent. His second thesis examines the advantages and disadvantages of the market economy concretely and promotes the 'Social Market Economy' as the appropriate vehicle for economic reconstruction.

The formulation of the Social Market Economy

Why should the Social Market Economy—the focus of the second part—be the preferred economic order? Why not merely a 'market economy'? Müller-Armack points out that: 'The matter of economic order relates closely to the problem of political order and the whole life order which

we aim for. It is obvious today that it is impossible to realize the ideals of human freedom and the dignity of the individual so far as the economic order which we chose contradicts them' (p. 81). The thought pattern characteristic of ordoliberalism is apparent here. Müller-Armack considers freedom as a supreme value; he rejects the economic order that opposes freedom from the viewpoint of the 'interdependence of orders'. Once again he refers to the issue of economic control in the light of this larger principle. According to 'the internal logic of the control system' (p. 82), this system must resort to the most extreme coercive measures. Obviously, this recognition is based on the interference theory of von Mises. For Müller-Armack, this was confirmed by the economic control of the past ten years or so. He writes: 'Because the failure of economic control is clear, all the assertions which make the people expect that this order can be improved in the future ignore the basic fact that economic control makes instability the substance and brings finally the condition of non-freedom to the whole' (p. 82).

Economic control is the problem of power because a state uses it as an instrument which ultimately dominates the forces of the national economy. Such an instrument must damage human freedom. Here, he cites Montesquieu's assertion that the division of power is indispensable to the success of freedom. Müller-Armack thinks that this assertion is applicable not only to political power but also to economic power. Economic power is one form of power, and it always entails the danger of abuse. But, in contrast to economic control, the market economy meets the requirement of Montesquieu because economic superiority is no longer a factor and no one is supposed to be able to dominate the others. So far as it has such a principle, the market economy is considered as the 'security which assures individual freedom'. That is, Müller-Armack's biggest concern is securing freedom, and it is condensed in one sentence: 'Even if economic performance is inferior to economic control, the market economy must be chosen from the viewpoint of freedom' (p. 84).

After rejecting economic control, Müller-Armack proceeds to examine the market economy. In so doing, he considers the market economy only in its instrumental aspect. How is such an approach possible? Müller-Armack regards freedom as an absolute condition in the choice of economic order. For him, no economic order is distinguished by its ultimate goal, because the ultimate goal of all economic orders is to ensure the economic welfare of all classes. This means full employment so that work and food are available to everyone. Therefore, the instrument chosen to attain that goal is critical. It is no longer a question of ideology. There remains only 'the problem as a mere instrument' (p. 85).

Then what are the characteristics of the market economy as an 'instrumental order'? What is the problem if this order is not perfect? Müller-Armack pays attention to certain functions (or attributes) of the market economy and emphasizes its characteristics as an 'instrumental order'.

From the viewpoint of sociology, Müller-Armack argues, the first function of the market economy is to prevent the emergence of power in the economy. Certainly, as was illustrated by the development of monopoly in the last century, market does not always discharge the function in reality. But this does not deny that the market economy has the social function of controlling the market power. Insofar as the market economy has such a function, Müller-Armack thought that it could be combined with the political form of liberalism.

It is wrong of him to equate the market economy with economic liberalism, however. Historically, the market economy has existed in various forms. It could appear anywhere if the control device of economic policy was absent. He thus gives the attribute of the 'organization principle which has been used in almost all ages' (p. 90) as the second characteristic of the market economy. He admits the historical character of liberalism: 'What has been added to liberalism in the eighteenth and nineteenth centuries was the understanding of the function of the market economy as a means of organization. This made it possible to mold the function clearly, and the economic order was combined with the various principles of political liberalism' (p. 90). The organization principle is an attribute of the market economy, and it is never a creature of liberalism. Therefore, that the principle of the liberal market economy was defective does not mean that the market economy *per se* should be denied. Müller-Armack considered the organization principle of the market economy to be universal.

The third function is that the market economy exists as one economic order. Every economic phenomenon in the market economy is ruled by consumption. Consumption gives production activities a decisive signal by expressing value-evaluation in prices. The purchasing power of the consumer comes from the income earned in the market. The market economy is able to perform because of the free formation of prices and the free disposal of income. The market economy as a 'highly rational economic calculation system' is based on a framework created through the distribution of income (p. 91). In a framework of the market economy, changes in demand and supply of goods occur promptly in accordance with the changing availability of goods. Consequently, the economic calculation system gives each phenomenon economic transparency and then stimulates economic exchange. Müller-Armack believes that the exchange structure supported by the economic calculation system is the essence of the market economy. Thanks to this exchange structure, the consumer takes a great interest in economic efficiency and cooperates with its advances voluntarily. It is the lack of an accurate economic calculation system that characterizes the controlled economy, and Müller-Armack sees an essential limitation of that economy in this fact.

Individual freedom is indispensable to the development of the market economy. Competition, which necessarily occurs under freedom, is a

fundamental principle of the market economy and Müller-Armack's fourth function. He explains the meaning of the 'competitive' principle as follows: 'Interest in the distribution of goods corresponding to the result of labor will be raised by competition. Competition forces individuals to increase their achievements. They must do so to guard their position' (p. 93). Competition not only draws out and organizes individual abilities. Müller-Armack suggests that the 'competitive system' of the market economy also serves the public interest by curtailing monopolistic exploitation through the intensification of competition.

The principle of competition, however, is not inherent in the market economy itself. Müller-Armack believes that insufficient consideration of this principle is one of the causes of the failure of the liberal market economy. The problems of the liberal market economy should be stated with accuracy. The market economy changes variously according to conditions, although the 'organization' principle is certainly universal. The liberal form of the market economy was artificial because it was, as it were, 'a grafted form of the market economy which grew by itself' (p. 100). In other words, although various principles such as price formation and the exchange of goods had been used thus far unconsciously, the notion of the liberal market economy grasped them theoretically and used them consciously to reshape the existing economy as a pure market economy.

The molding of the market economy as an order was started under liberalism. Liberalism aimed at scrapping the economic constraints of mercantilism so that it could enjoy the fruits of the natural economic order. Principles such as free trade, the freedom of business, and the gold standard were established for that purpose. Liberalism was considered to be sufficient for the whole order only by the 'guarantee of the formal political constitution' (p. 105), and such a constitution was actually enacted. This fact obviously shows the intensity of liberalism's discredit of the state. But Müller-Armack suggests that the danger of discredit was too great. Is the order of the market economy established once the right of competition is formally guaranteed? Of course, his answer is in the negative, based on the following diagnosis: 'The market economy of *laissez-faire* did not lead to real competition, at least in Germany, and it reverted to the traditional restraints' (p. 118).

The legal framework for guaranteeing competition is substantially missing from the liberal market economy. The need for it has not been recognized from the beginning. Müller-Armack tries to understand this deficiency in the liberal market economy by means of liberalism's own ideology. In the first place, liberalism accepts the notion of preordained harmony. For economic liberalism, the result of the process of the market economy is preordained and therefore the result is ultimately right. The competitive order is considered as the natural form, and intervention in this order is denied by the state. According to Müller-Armack, 'The instrumental

character of the order established by itself was mistaken for liberalism because of ideology, and the market economy was seen as the autonomous world.' In other words, his criticism is that liberalism tried to make the market economy 'the idol of its own ideology' (p. 107).

Next, Müller-Armack raises the problem of the choice of economic order again. For him, both the liberal market economy and economic control are unacceptable. But the original molding power of the market economy was not exploited fully under the liberal market economy, which was only one form of the market economy. Müller-Armack thus proposes a 'Third Form' or a 'Third Way'. This is not a mixture or a compromise, but rather a synthesis obtained through the best insight available. Müller-Armack calls it the 'Social Market Economy' and defines it as follows: 'We think that the market economy is the basic framework for the future economic order. But it must not be a liberal market economy left alone. It should be a market economy consciously guided, that is, a socially guided market economy' (p. 109).

He explains the characteristics of the Social Market Economy rhetorically:

> Even the best machine will require meaningful human operation. The price mechanism is the same, too…. It is foolish to refuse to use a machine just because the machine was not used properly and stopped moving once. In so far as the fully automatic machine is not invented, …it is important to develop economic policy that is oriented toward meaningful control of the exchange economy of the unique organizing device.
>
> The guided market economy is distinguished from both the liberal market economy and economic control. We do not think that it is suitable to let a machine work at full speed like the supposition of liberalism. We do not think that what was done by economic control is suitable: all the safety valves were tightened, and all the handles were fixed. We try to give the machine the flexibility that is necessary for the gear and safety device so it will produce a rational result.[8]
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> (Müller-Armack 1966:77).

The Social Market Economy as a style

How should economic policy be made in a Social Market Economy? It cannot be said that Müller-Armack fully answers this question. For example, although he raises Röpke's idea of 'market conformity', he does not search for a concrete economic policy corresponding to this idea, but only shows the general aim. His argument appears only to summarize the arguments of other Ordoliberals. But he puts a strange argument in the summary discussion. Although economics scholars hardly pay any attention to this argument, it can be said that it gives his concept of Social Market Economy originality. Therefore the meaning of this argument should be explained.

Müller-Armack discusses the requirement that the market economy should become stable in his chapter entitled 'The Molding of the Economic Structure.' At the beginning, he removes any doubts of his own: 'Can we acknowledge an intrinsic order of the market economy? We can probably answer this question affirmatively only when we know that our belief in life (Lebensüberzeugungen) is secured in the order' (p. 126).

How should this argument be interpreted? For him, the market economy is an instrumental order, that is, a means to achieve economic order. Naturally, the means is different from the end. What is the end if the market economy is a means? It is a 'belief in life'. Therefore, he states that we can probably make the final decision about the market economy only when we can believe that the market economy realizes the 'value of the order of life as a whole' (p. 126). Then what is the implication of terms such as a 'belief in life' and the 'value of the order of life as a whole'? Do they mean the 'value of freedom' treasured by liberalism? Clearly he attaches importance to freedom as an ultimate value. However, what he conjures up here is more fundamental—as if it were something metaphysical.

The economic order, which is a formal system, cannot create a 'belief in life' as an end in itself. The end must be, as it were, always imposed on the economic order from the outside, and the economic order can last in the long run only in such a case. However, the Classical Liberalists made the relations between the end and the means vague by taking the order of the market economy as the 'order of life as a whole'. Müller-Armack considers such a misunderstanding to be natural historically because the mentality of the Christian legacy from the economic life of the nineteenth century still existed. The liberal market economy could become comparatively stable in the long run if it were rooted in the unconscious mentality. However, conditions in the twentieth century are different. Such cultural tradition has already been exhausted. The purpose of life is lost sight of, and the economic order as a means works recklessly. It is the age of social crisis.

Müller-Armack's grasp of the crisis is significant. Not only does he protect the market economy but he also emphasizes that 'the mental molding of the market economy should be conducted on a large scale now' (p. 127). This argument proves that he thinks that a kind of mental support is indispensable to the stability of the Social Market Economy. More specifically, he appears to be requesting regeneration of faith. This is implied in his next sentence: 'The history of cultural style tells us how many historical forms are maintained when the unification of style spreads to all areas of life' (p. 89). If the concept of style is to be included in the argument, his 'Social Market Economy' will have to be formed as a 'style'.

For ordoliberalism, the creation of the competitive order is a political task. Suppose that the building of an institutional framework is indispensable to the creation of the competitive order, a state is expected to be sufficiently

great to bear such a task. Müller-Armack expects a great state. However, his interest is in not only the creation of the order but also its maintenance. For him, ordoliberalism is only a part of the requirements for the maintenance of the order. In the Social Market Economy the competitive order lasts in the long run, and he thus requires that the economic order is put together as a unified order of whole life through 'belief in life'. Although he only refers to 'style' in one sentence in his *Wirtschaftslenkung und Marktwirtschaft,* the thought of 'style' also took a back seat in his 1941 book *Genealogie der Wirtschaftsstil,* which is considered to be his most important work. He probably avoided going into the problem of 'style' in detail because it far exceeded the scope of economics. However, neither could he completely omit style from his notion of the Social Market Economy.

The argument in *Genealogie der Wirtschaftsstil* needs to be explained to properly analyze the implications of the Social Market Economy as a style.[9] This book is, as it were, the monograph of self-criticism of Müller-Armack, who had been the only member of the Nazi Party among the Ordoliberals. He expected that National Socialism—or more precisely, Italian fascism—would provide the energy to regenerate an almost dying market economy. Soon losing his enthusiasm for National Socialism, he changed the object of his own research from economics to cultural sociology and anthropology. The result was *Genealogie der Wirtschaftsstil,* subtitled 'The Origins of Political and Economic Forms until the End of the Eighteenth Century as Seen from the Viewpoint of the History of Thought'.

Müller-Armack's motif is to eliminate the dualism between religion and the economy through an understanding of capitalism by the latest advocates of the German Historical School such as Werner Sombart and Max Weber. That is, economic style as a sphere of life is supposed to be fundamentally controlled by the ideology of religion, and the proof is found in the gradual development of European history. Though the main subject is European economic style in modern times, the prehistory of economic style is presented as the 'genealogy of early economic style'. The history of mankind as seen from the world of faith and such concepts as the 'image of the magical world', 'animism', 'polytheism', and 'monotheism' is sketched here. Only the monotheism of medieval Europe discarded ceremonialism or ritualism, and economic ethics took its place; then economic style was formed as a cultural style on the basis of this religious consciousness. Although the discussion of the prehistory of economic style is brief, European medieval economic style is examined in greater detail. Finally, modern European economic style is discussed.

Modern economic style is supported essentially by the religious consciousness of Protestantism, especially the dynamism introduced by Calvinism. Therefore, modern economic style should be distinguished from the medieval one that appeared throughout Western Europe. Müller-Armack thus examines the regional differences of modern economic style. But his

assertion is not mere determinism. For instance, he thinks that the economic style of Prussia, which played an important part in modern German history, originated in a combination of Calvinism and Lutheranism. In other words, he recognizes the significance of the peaceful coexistence of religious faiths.

History after the nineteenth century is in principle outside the scope of his study. Nevertheless, he does discuss the problem of post-nineteenth-century vulgarization. Müller-Armack sees the ultimate cause of the crisis in modern society in 'vulgarized attitude' (1981b:47). Vulgarization, that is, the weakening of religious consciousness, is understood as the complete breakdown of modern economic style. The appearance of a cold-hearted, rational dictator, for example, cannot be understood if the conditions producing the loss of 'belief in life' are not considered. How can this serious crisis be overcome? It seemed insufficient to him that only a political base was established to build the desirable economic order. Müller-Armack argues that the individual's mental independence must be considered because the fundamental cause of the crisis is not politics and the economy but the mind. But what makes such independence possible on earth? It is a contradiction in terms to force independence politically, and it must be avoided in the first place. Although obviously it is a dilemma, Müller-Armack does not pursue the subject. Probably, he thought that a breakthrough could be achieved only in a movement like the rebuilding of faith.

Conclusion

Müller-Armack published a small article entitled 'Stil und Ordnung der Sozialen Marktwirtschaft' in 1952. Here the implications of the term 'Social Market Economy' are expressed in a straightforward way. His 'Social Market Economy' must be understood from the viewpoint of both 'style' and 'order'. Economic reconstruction progressed rapidly in West Germany after the currency reform of 1948. Müller-Armack recognizes that the formation of the 'order' of the market economy is based on a similar reality. But the formation of the 'order' is only one of the requirements for his molding of the 'Social Market Economy'. The order's integration in the order of life as a whole is more important. In other words, he thinks that the Social Market Economy is completed as a 'style' by such unification. The route to unification must be the problem. Emphasis is put on the 'regeneration of value' (Müller-Armack 1966:238) as a premiss of unification. After all, his argument ends in the expectation of the revival of religion or faith. Only the energy that comes from religion can produce the regeneration of value. This is the conclusion of his argument about the 'Social Market Economy as a style'.[10]

Müller-Armack's concept of the 'Social Market Economy' was based on his criticism of the economic control of the Nazis. As for his assertions about economics and economic policy, he summarizes only the various concepts

that had already been brought forward by the new liberalises, who assumed a negative attitude to the tradition of the German Historical School. The originality of his concept is in his philosophical argument of the 'style' developed by the historical and ethical method in the tradition of the German Historical School. He let his own value-judgment dominate in the argument concerning the meaning of the whole of social existence. His conclusion is seemingly very conservative. However, it should not be understood as a recurrent assertion of the tradition because it is a reaction to the fundamental crisis of modern society. The German Historical School did not separate learning and politics. It was probably to follow such a tradition that he repeated its language and behavior in order to draw the Social Market Economy closer to the ideal.

Notes

1 E.g. Tribe (1995:203–8) tries to interpret the meaning of the Social Market Economy as a 'political slogan'.
2 Müller-Armack was known only for coining the phrase 'Social Market Economy', and his actual arguments were hardly examined. Recently, however, scholars have given his work more attention. See Nicholls (1994) and Koslowski (1998). The research of Haselbach (1991) is especially valuable in clarifying Müller-Armack's activities in wartime.
3 The argument of von Mises (1922) was developed as a comprehensive critique of socialism.
4 The *Ordo* bulletin, edited by Eucken and Franz Böhm, was subtitled *Jahrbuch für Ordnung von Wirtschaft und Gesellschaft*. Some people may associate Max Weber's *Wirtschaft und Gesellschaft* with this subtitle.
5 See, e.g., the title of Haselbach (1991).
6 These proposals are found in Müller-Armack (1981a).
7 In fact, *Wirtschaftslenkung und Marktwirtschaft* was published in 1947. December 1946 was the date which Müller-Armack wrote in the 'preface' of this book.
8 Admittedly, Röpke (1937) influenced Müller-Armack's argument.
9 My commentary is based on Haselbach (1991:117–58).
10 'Style' is a problem only at the level of the national economy. There is even a problem with the unification of a big economic space like European integration. See Müller-Armack (1956).

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