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A Realist Political Economy and Moral Philosophy: Smith and Mittermaier

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Abstract

In the *Theory of Moral Sentiments*, Smith argued against the account of human nature which views moral sentiments as deriving from self-love. This paper emphasises that Smith's understanding of human nature was not that it was either selfish or benevolent. Human nature consists of the ability to be either or, and the three powers of the mind actualise this ability. The powers of the mind are will, intellect, and memory, to which correspond respectively the offices of self-command, sympathy, and the impartial spectator. The system of sympathy is an example of what Mittermaier calls an ex-ante fact and allows for a real distinction between vice and virtue. Other distinctions important to Smith include production versus predation and market price versus natural price. This paper develops a model that brings together these real distinctions. It demonstrates the complementarity of the *Theory of Moral Sentiments* and the *Wealth of Nations.*

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1. Introduction

Realist in the title of this paper means that for Adam Smith, certain distinctions are real and what is on either side of the distinction differs in kind from each other. Smith distinguished between i) vice and virtue, ii) production and plunder, iii) productive and unproductive labour, and iv) market price and natural price. While Smith is considered the father of economics, economists have ignored or dismissed his four distinctions. Schumpeter, not an admirer of Smith in any case, expressed the modern view, referring to the "meaningless discussion" of the distinction between productive and unproductive labour that "became a standard item of nineteenth-century textbooks despite the increasing awareness of its futility" (1954, 631). In this, he saw a "word-mindedness" and an inability to tell a real problem from a spurious one.[1] This article argues that important insights have been lost by abandoning Smith's real distinctions and by condemning them as word-mindedness.

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[1] See Bladen 1960.

The distinction between vice and virtue is featured in the *Theory of Moral Sentiments* (TMS), whereas the other three distinctions appear extensively in the *Wealth of Nations* (WN). This article brings together the four sets of distinctions into a coherent whole. On the one hand, the conduct of individuals, virtuous or defective, has macroeconomic consequences, affecting the wealth of nations on the other hand, and vice versa. In contradistinction, in modern textbook economics, differences in kinds of conduct are eliminated. All conduct is regarded as self-interested and based on rational choice.

In this article, the four distinctions will be set out within Mittermaier's conceptual framework of ex-ante and ex-post facts, which will be introduced in section 2. Sections 3 to 5 discuss the understanding of human nature and self-love found in Smith's TMS. Smith argued against the view that our moral judgments have their origin in self-love. He did not consider human nature to be either selfish or benevolent. Instead, *sympathy*, *the impartial spectator*, and *self-command* form an ex-ante framework that actualises the ability to engage in either selfish or benevolent conduct. The three concepts are instances of the three powers of the mind: will, intellect and memory.

Section 6 explains why, considering the preceding, there is no Adam Smith problem. It clears the way to appraise TMS and WN as constituting a coherent whole. In both books, there is found an ideal, discussed in sections 7 and 8, which together give impetus to a classical liberal political economy and a realist moral philosophy. Using a zig-zag diagram in section 9 similar to that pioneered by Witztum (2016) (also in the context of Adam Smith's TMS), it can be portrayed schematically, where the four distinctions are represented along the four sides. The connections they represent are not meant to be logical connections. They are empirical connections with realist relevance. Section 10 concludes by proposing a moral philosophy and political economy index based on the model developed in section 9.

2. Ex-Post and Ex-Ante Facts

Mittermaier (2023) develops a conceptual scheme differentiating between ex-ante and ex-post facts which helps us to see Smith's four sets of distinctions in a novel way. Ex-post facts are in the order of facts that lie in the past, whereas ex-ante facts persist over time. The distinction can be illustrated based on the 1930s story of bank robber Willie Sutton. When finally caught, and according to a newspaper reporter, Sutton was asked why he robbed banks, to which he replied: "Because that is where the money is." The joke in this was appreciated in the popular press and morphed into "Sutton's law" which states that one should first consider the obvious when diagnosing.

The example provides two ex-ante facts and two ex-post facts. First, the fact that the money is in the bank is an ex-ante fact. It still is to this day. Second, Sutton could also have replied "Because I want to," which also refers to an ex-ante fact: he had the will to do it and continued having that will, committing further robberies. The human will is something we have, and it is not the same as choice, which occurs in time. The will, persisting over time, is an ex-ante fact. A choice is an event that occurs but passes as it occurs. It is in the realm of ex-post facts. In the Sutton example, the two ex-post facts –

records of past events – are i) that he robbed a bank on such and such a day, and ii) someone suffered a financial loss on that day. Fact i) is a choice and ii) the effect of the choice.

The facts also correspond to Smith's four sets of distinctions: i) Sutton's labour was unproductive on Smith's definition of it; ii) those who suffered the loss received no commensurate price; iii) those who persecuted Sutton served institutions that abjured plunder; iv) Sutton's will prompted him to towards a defective act. The details involved in i) and ii) show them to be in the order of ex-post facts; those for iii) and iv) are in the order of ex-ante facts.

In the WN, Smith discusses various institutions, which are instances of ex-ante facts. In TMS, Smith is equally concerned mostly with ex-ante facts: the principles by which we judge the conduct of others and, by implication, the principles we use to judge our own conduct. Further down in this article, a model bringing together these two types of ex-ante facts will be developed. The other two distinctions are in the order of ex-post facts. Thus, productive/unproductive labour and natural/market prices will be treated as ex-post facts.

The distinction between ex-ante and ex-post facts is important for an understanding of the differences between Smith, on the one hand, and Hobbes, Hume, and Mandeville, on the other. The latter three represent the view that all conduct is based on self-love. This view leaves little room for distinguishing between virtuous and defective conduct. All human conduct is of one kind: based on self-love. If there are differences, these are expressed as differences in their effects rather than differences in kind.

To illustrate, in the economic literature on altruism, the altruist is thought to receive utility and thus serves his self-interest by acting altruistically. His altruistic conduct is not different in kind from his selfish conduct; both are self-interested. They differ in their effects. The self-interested acts that benefit others may be classified as altruistic, and the self-interested acts that wrong others may be classified as selfish. It is an ex-post classification that occurs after the event.

This is akin to the study of externalities, where a firm's wealth-maximising choices may have positive or negative external effects which become evident ex-post. So, while the altruist might regard his act ex-ante as benevolent, the act is simply self-interested from the observer's perspective. After the event (viz. ex-post), an observer may classify the acts as virtuous or vicious, depending on their effects. This view is beautifully encapsulated in the subtitle – "Private Vice and Public Virtue" – that Mandeville chose for his *Fable of the Bees* ([1714] 1988). An individual can commit a vice, but it may be considered a virtue if it has positive effects.

Smith argues against this view (*e. g.*, in the chapter "Of those Systems which deduce the Principle of Approbation from Self-love", TMS VII.iii.1). The problem with Hobbes, Pufendorf, Mandeville, and Hume (though Smith does not mention Hume) is that they fail to understand the role of sympathy, which "cannot, in any sense, be regarded as a selfish principle" (TMS VII.iii.1.4). Smith considers not the ex-post effects of human conduct but the ex-ante "system of sympathy" (TMS VII.iii.1.4) and other powers of the mind.

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3. Smith on Human Nature

Smith explicitly disapproved of the argument that placed self-love at the heart of human nature: "That whole account of human nature, however, which deduces all sentiments and affections from self-love, which has made so much noise in the world, but which, so far as I know, has never yet been fully and distinctly explained, seems to me to have arisen from some confused misapprehension of the system of sympathy" (TMS VII.iii.1.4).

But what is Smith's account of human nature if the self-love account is wrong and human nature cannot be reduced to self-love? If TMS and the WN are to be accepted as a cohesive whole rather than as opposing pieces, this question must be addressed. The overall objective of this paper is to establish a realist political economy and moral philosophy in which virtue and vice and institutions are considered real ex-ante facts, not treating them as just ex-post classifications of merely self-interested conduct. However, the two parts of Smith's system cannot be combined if they have contrary assumptions about human nature.

In modern economics, we are prone to reduce human nature to the pursuit of self-interest and interpret the WN as an application of the self-interest assumption. In the past, amongst economists, the predominant view was that Smith changed his mind about self-interest between the publications of his two books. According to this view, TMS assumes that human nature is benevolent, while when he wrote the WN, Smith assumed human nature to be self-interested. This view has been debunked many times over, more so by philosophers than economists.

In fact, human nature is not self-interested or benevolent. Instead, our human nature consists of the *ability* to be either self-interested or benevolent. This seems to have been Smith's view when he wrote that "to restrain our selfish, and to indulge our benevolent affections, constitutes the perfection of human nature" (TMS I.i.5.5). To paraphrase Smith's sentence, human nature is such that we can either restrain or not restrain self-interest and indulge or not indulge our benevolent affection. Human nature can be actualised in one manner or the other.

However, what is generally meant by *nature*, be it human nature or some other nature? The word has many meanings, but the one appropriate here is best understood in Aquinas' definition: "Nature is the beginning of those things that can only be thus." A pumpkin seed can grow only into a pumpkin; it cannot grow into something else. Berquist (2005) develops this into the expression that what is natural is "determined to one." For example, humans seek happiness; we do not seek its opposite: wretchedness. However, seeking our own happiness does not imply only selfishness, for we can find happiness in our benevolent or selfish conduct.

Some interpret Smith as holding a view of human nature that comprises two parts: the benevolent and the selfish. This defies the ordinary meaning of nature, where in this context it means "determined to one." It is even contradictory, and it was held against Smith by the German Historical School. However, Smith's formulation makes it clear that he did not consider the one or the other of the two opposites to be our human nature. Thus, he thought Hume erred in reducing all our conduct, including virtuous conduct, to self-love. Equally, he thought Hutcheson erred in thinking we have a

natural moral sense that is the source of our benevolence. Smith was not finding a middle ground between the two. Instead, he wanted to shift the conceptualisation onto an entirely new ground.

In formulating human nature as the ability to be either or, the either-or does not refer to the ability. It is not the case that we either have the ability or do not have the ability. Human nature is that we have the ability; it is ordered to one that we have the ability. However, if there is such an ability, there must also be something that actualises or gives life to that ability; something that, to use Smith's expression, "constitutes the perfection of human nature" (TMS I.i.5.5). There needs to be some power that actualises the ability. In this regard, Smith uses the expression of "the power or faculty of the mind," which is discussed in the next section.

4. Three Powers of the Mind

Haakonssen (2002, vii) summarised the general argument found in TMS in a way that echoes the ex-ante and ex-post conceptual framework: "Smith analysed those *features* of the *human mind* and those *modes of interaction* between several minds which gave rise to moral practices in the *human species*" (italics mine). The actual acts are instances of ex-post facts that occur against the backdrop of the ex-ante facts (the italicised words), which are the features of the human mind and modes of interaction. In what follows, I shall not use Haakonssen's expression of the "features of the mind"; instead, I will use Smith's expression "power of the mind": in the lead-up to his critique of Hobbes, Mandeville, and Pufendorf, Smith explains his purpose to identify "the power or faculty of the mind" based on which we judge our conduct and other's conduct as right or wrong.

> After the inquiry concerning the nature of virtue, the next question of importance in Moral Philosophy, is concerning the principle of approbation, concerning the *power or faculty of the mind* which renders certain characters agreeable or disagreeable to us, makes us prefer one tenour of conduct to another, denominate the one right and the other wrong, and consider the one as the object of approbation, honour, and reward; the other as that of blame, censure, and punishment (TMS VII.iii.intro.1, italics mine).

He discusses and then rejects the three candidate grounds for our judgements: self-love, reason, and moral sense (feelings or sentiments). In their place, he argues in favour of *sympathy* as the power of the mind that accounts for our judgement of conduct as right or wrong.

To fully account for our conduct, in addition to sympathy, Smith brings into play two further powers of the mind: the impartial spectator and self-command. Smith did not interchangeably use the two expressions of sympathy and the system of sympathy. The latter had a more extensive meaning. In what follows, the *system of sympathy* shall refer to the triplet of sympathy, the impartial spectator, and self-command. In his system of sympathy, the *impartial spectator* and *sympathy* was, for Smith, central to his argument from the book's first publication. The role of self-command, on the other hand, acquired increased prominence in subsequent editions. "But" observes Montes (2020, 121), "the relevance of self-command […] has been rather neglected"

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by commentators even though in the new part of the sixth edition of TMS, Smith emphasises the importance of self-command.

This section will draw attention to Smith's triplet in the system of sympathy as three separate powers of the mind. These powers of the mind give life to the ability to behave selfishly or benevolently. These three powers are pertinent in moral sentiments but may be irrelevant in other contexts. For instance, when one plays a competitive chess game against a computer, neither sympathy, self-command, nor conscience comes into play. In the context of the full range of human endeavours, there must naturally be many more powers of the mind.

The full range of different powers of the mind can be subsumed under three headings, which are i) the will, ii) the intellect, and iii) the memory. In a chess game, for instance, i) the will seeks victory, ii) the intellect thinks many moves ahead, and iii) the memory recalls past games and probable outcomes. In the context of Smith's TMS, the three powers of the mind act as follows: i) the will enjoins self-command, ii) the intellect contemplates sympathy, and iii) the memory brings to mind the impartial spectator and its associated habits and rules of conduct.

In the same section of TMS, where he argues against Hobbes' attempt to equate moral conduct with political reasoning, failing to recognise sympathy, self-command and habit, Smith refers to "the distinct *offices* and powers … of the human mind" (VII.iii.2.5, italics mine). Accordingly, the terminology to be adopted here is as follows. The powers of the mind refer to the three generic powers of the mind: i) will, ii) intellect, and iii) memory. Offices of the mind shall mean instances of generic powers. Thus, self-command in moral considerations and victory in chess are two offices (there are many more) of the will. Sympathy and thinking ahead are offices of intellect. Impartial spectator and recall of past games are the offices of memory.

The three powers of the mind and their offices of sympathy, impartial spectator and self-command are examined in more detail hereunder. In order to show that people are more than the self-centred creations that Hume and Mandeville imagined, Smith establishes *sympathy* and the *impartial spectator* as the central elements of his moral philosophy. Both concepts he regards as his original contribution to the subject.

Sympathy, as suggested above, is an office of the intellect. It is the ability to put oneself into the shoes of another. It is an intellectual exercise and, as such, an act of intellect. Montes recently emphasised this: "Even though TMS is about sentiments and passions, sympathy requires reason" (2020, 123).

The impartial spectator is an office of memory. Our ability to judge our actions more accurately depends on the imaginary observer, serving as a sort of conscience. However, this observer is based on experience through which we develop general rules of conduct. On these we rely "in correcting the misrepresentations of self-love concerning what is fit and proper to be done in our particular situation" (TMS III.4.12). It is not reason, as Plato had argued, that furnishes us with the correct rules of conduct, but they become established by learning and reinforcement. The impartial spectator, therefore, repeatedly invoked in guiding our behaviour, is an act of memory.

Self-command is an office of the will. It means control of our behaviour and emotions. Awareness of the impartial spectator teaches us to practice restraint and self-

command. When we do this under severe duress, we demonstrate magnanimity. Self-command, Smith observes, "is not only itself a great virtue, but from it all the other virtues derive their principal lustre" (VI.iii.11).

Self-command as an office of the human will has come to the fore in recent work, where it is argued that the Smith scholarship (Raphael and Macfie ([1976] 1982) in particular) has overestimated the stoic aspect of Smith's notion of self-command. Montes argues that "what distinguishes Smith's self-command from simple Stoic self-control is that 'command' gives this virtue a sense of direction […] it relates to what not to do, but also to what *to* do" (2020, 132). It gives self-command the hallmarks of a virtue, making every act of self-command a choice for the good. Self-command is, therefore, a virtue and the prerequisite for other virtues. As a prerequisite for virtue, self-command is associated with rational action. As a virtue, self-command is associated with human autonomy, choice, and free will. Carrasco (2012, 393) highlights connections between TMS and Frankfurt's notion of true freedom of the will, which is about the "desires we choose to desire," as opposed to "desires that follow from our natural sensibility." The latter is qualified as pre-moral self-command, the former as moral self-command: "Self-command embodies free human choice […] or autonomy" (Carrasco 2012, 399).

5. Self-Love, Self-Interest and Selfishness

A different and related perspective on the distinction between moral and pre-moral self-command is offered here, which helps to clarify the differences between self-love, self-interest, and selfishness. This distinction is crucial for understanding Smith's critique of those who dismiss virtue as a genuine phenomenon, instead attributing all behaviour to self-love.

There are two aspects to the will as a power of the mind. One may distinguish between "will as nature" and "will as will," a distinction brought out by Berquist (2005). As nature (and determined to one), the human will desires happiness and desires to live (or at least to live not wretchedly). "One of the most important principles in human nature", writes Smith, is "the dread of death, the great poison to the happiness" (TMS I.i.1.13). However, "will as will" (as opposed to "will as nature") can direct action down many different paths. "Will then is a beginning of those things which are able to be thus or otherwise" (Berquist 2005, 21). The human will, so to say, is the depository of all the works of man. Thus, the human "will as will" – not as nature – determines whether we engage in conduct that is either virtuous or defective. Some people commit suicide not because they do not want happiness or do not want to live but because they cannot find happiness and do not want to live wretchedly. Suicide does not go against the "will as nature": it is the "will as will" that directs its action to suicide.

The "will as nature" corresponds roughly to what Carrasco (2012) calls pre-moral self-command. It seeks happiness, but how that nature expresses itself can differ vastly: the "will as will" seeks that happiness in many possible ways, some virtuous, some vicious. It is the "will as will" (what Carrasco calls the moral self-command) wherein

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lies the actualisation to act benevolently or selfishly. It is not human nature but the human will which contains the seed of all evil.

The concept of "will as nature" allows for a re-evaluation of Smith's rejection of Hume's and Mandeville's account of human nature, according to which all sentiments and affections derive from self-love. Smith distinguished between the notions of self-love, self-interest, and selfishness. As used by Smith, self-love refers to the natural preference individuals have for their own happiness; self-love, like happiness, belongs to the confines of "will as nature" or pre-moral self-command. There are proper bounds to this self-love, and the system of sympathy monitors those bounds. In the extract below, Smith points to the impartial spectator, the man within, as keeping self-love in its proper place: "When the happiness or misery of others depends in any respect upon our conduct, we dare not, as self-love might suggest to us, prefer the interest of one to that of many. The man within immediately calls to us, that we value ourselves too much and other people too little, and that, by doing so, we render ourselves the proper object of the contempt and indignation of our brethren" (TMS III.3.5).

Conversely, self-interest (as opposed to self-love) belongs to "will as will" and is inherently neutral (Smith's propriety); but it can manifest itself as either selfishness, a vice, or public-spiritedness and industriousness, which are virtues. Whether one's self-interest is steered towards vice or virtue or is kept neutral is determined by one's moral self-command, or "will as will."

Smith critiques philosophers like Hume and Mandeville for failing to confine the meaning of self-love to "will as nature." Instead, they incorrectly extend self-love to encompass the motivation behind all human actions, whether altruistic or malevolent, virtuous or vicious, effectively equating it with "will as will." This conflation blurs the distinction between self-love and selfishness, making them appear as mere degrees of the same phenomenon.

For Smith, the difference between self-love, on the one hand, and selfishness and self-interest, on the other, is a fundamental difference in kind. Our self-love and desire for happiness are necessities, not choices, and constitute our "will as nature." In Smith's system of sympathy, self-love assumes its rightful role as an inherent aspect of human nature that lies beyond the realm of choice, yet does not dictate choice. In contrast, our self-command to deny or indulge in improper actions involves a choice, exercising our "will as will." By distinguishing these aspects, Smith provides a clear understanding of human nature, acknowledging the potential for both virtue and vice within the framework of self-interest.

In summary, Smith's conception of human nature may be portrayed as follows: By nature, humans seek happiness and possess self-love. But by nature, they are neither selfish nor benevolent. They can be either or not, but to actualise the ability the "will as will" is required. Human nature comprises the body and mind, with three powers: will, intellect, and memory. The power of the human will (through the office of self-command or its absence) can actualise the ability and give life to a benevolent or selfish act. In Smith's system of sympathy, sympathy and the impartial spectator help to keep self-love ("will as nature") in its proper place. He sets right that mistaken "account

of human nature […] which deduces all […] from self-love, […] arisen from some confused misapprehension of the system of sympathy" (TMS VII.iii.I.4).

6. Das Adam Smith Problem

This interpretation of human nature and mind, along with the three powers of will, memory, and intellect, aids in resolving one of the perennial puzzles in Smith's work. The first sentence in the TMS has attracted much debate and little understanding. "How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others" (TMS I.i.1.1). Familiarity with the "Adam Smith Problem" may prompt the reader to believe that in this sentence, there is already an expression of the tension between selfishness on the one hand and care for others on the other.

Therefore, many formulations argue that Smith's notion of human nature was contradictory or that it changed over time. Otteson (2000, 69) makes a modern rendition of the issues: "The Adam Smith Problem is not of merely historical significance. It is also a problem today because it highlights the tension between moral injunctions to beneficence and other virtues, on the one hand, and the apparent amorality of economic markets on the other." Buckle portrayed the matter as follows: "in the *Moral Sentiments*, [Smith] investigates the sympathetic part of human nature; in the *Wealth of Nations*, he investigates its selfish part" ((1861) 1903, 305).

In contradistinction, Smith saw no difficulty in his formulation and thought it sufficiently appealing to common sense to make it his first sentence in the TMS, the rest of which was to explain the matters raised there. Benevolence and self-interest are not two competing parts of human nature.

The resolution is as follows: the first portion of the sentence ("how selfish soever man may be supposed") refers to an act of the will. The last portion ("interest in the fortune of others") refers to an act of the intellect. The two parts, rather than being in opposition to each other, are coherent together. As an act of the will, one may act in varying degrees of selfishness without any impairment of one's interest in the fortune of others. As an act of intellect, interest in the fortune of others can be maintained even in the person who wills to act viciously selfishly. Of the three powers of the mind, the will is the most significant in our moral behaviour. "To restrain our selfish and to indulge our benevolent affections constitutes the perfection of human nature" (TMS I.i.5.5). It is a choice – an act of the human will – to act either in a selfish or benevolent manner.

Smith was hardly the first to express the matter in this way. The idea that there is no contradiction between being self-interested or even selfish, and yet being benevolent is as old as (and probably much older than) the book of Exodus (20:5). In the covenant with the people of Israel, God says "For I the Lord your God am a jealous God." Despite being jealous (therefore selfish), He also says, "I made you and will care for you" (Isaiah 46:4). There is no contradiction between jealousy and care. The first is an act of the will; the second is an act of the intellect.

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Moreover, philanthropy is based on the very idea expressed by Smith. The philanthropist's love for humankind is that of the rich person who selfishly makes and holds onto his riches. Coherence of character does not require greater care for others to be associated with lesser care for self. It is not a matter of moving along a mutually exclusive continuum. More germane would be the metaphor of a sailboat. One's self-command (the act of the will) steers with the rudder; sympathy (the act of intelligence) is the hull of the boat keeping the contraption afloat; the impartial spectator (the act of memory) is the sail, harnessing the wind (and experience) to gain momentum. All three components work together towards the destination set by the human will. A skilled yachtsman can even sail against the wind.

Neither benevolence nor selfishness are the nature of human nature, but they both presuppose a human nature. The distinction is analogous to the use of language. Smith writes that speech is "the characteristical faculty of human nature" (TMS VII.iv.25). While speech is part of human nature (belonging to our bodily abilities), language is not. We speak a particular language in a given country, not by nature but by custom. However, common customs presuppose a human nature with the powers of will, intellect and memory, allowing imitation and memorisation in the acquisition and use of a particular language. Analogously, we can acquire benevolence and selfishness through what is nature to us: the powers of will, intellect and memory. This squares with Smith's overarching argument that our modes of judging and our virtues are learned. They are not nature to us.

7. Ideals and Three Kinds of Acts

Mittermaier (2020 and 2019) interprets the WN as expressing an ideal of a free market economy. Pockets of actual free markets were discernible to Smith, but these were the exception rather than the rule, and on the whole, Britain was characterised by an absence of free markets.

Likewise, in TMS, Smith frequently distinguishes between the real or actual on the one hand and the ideal on the other. Raphael and Macfie, for instance, speak of "the dual character of his ideal" ([1976] 1982, 6), which consists of self-command and sympathy. "The man of the most perfect virtue […] is he who joins, to the most perfect command of his own original and selfish feelings, the most exquisite sensibility both to the original and sympathetic feelings of others" (TMS III.3.35). Evensky considers Smith's ideal of "the man of most perfect virtue," applying it to Smith's ideal liberal society that "would be inhabited by such perfectly virtuous beings. It would be a society in which all could enjoy liberty […] there would be no need […] to police, for in this perfect world citizens would know the ideal measure of justice and would have […] the self-command to enforce it upon themselves" (2005a, 118).

Aside from the ideal, Smith had no illusions that people generally do not conduct themselves with perfect virtue. He laments, in the subjunctive mood, that "[i]t were well for society, if, either mankind in general, or even those few who pretend to live according to any philosophical rule, were to regulate their conduct by the precepts of any one of them" (TMS VII.ii.4.5).

Adam Smith's name might be included in any list of major British empiricists of the 18th century. One may, therefore, wonder if it is legitimate to focus on the *ideal* in TMS. The *ideal* has connotations of the normative what ought to be, whereas empiricism is associated with positive statements of what is. Even in Smith's account, TMS is not about what ought to be but about what is the case. Thus, he writes: "Let it be considered too, that the present inquiry is not concerning a matter of right, if I may say so, but concerning a matter of fact" (TMS II.i.5.10). However, the matter of fact he refers to is not about how people behave. Instead, the matter of fact relates to the principles based on which we make judgements. "We are not at present examining upon what principles a perfect being would approve of the punishment of bad actions; but upon what principles so weak and imperfect a creature as man actually and in fact approves of it" (TMS II.i.5.10).

Smith may have no interest in finding out what may be an ideal way to judge, but he leaves a door open as to what may be ideal in terms of how to behave. This is not to say that Smith is a virtue ethicist, for he is not concerned with improving a person's character.

The following four aspects relate to Smith's understanding of virtue. First, in agreement with Aristotle, virtue is a matter of habit. An act repeatedly renewed forms the habit, and contrary to Plato, Smith affirms Aristotle's view that "good morals arose not from knowledge but from action" (TMS VII.ii.1.14). Second, Smith concludes that all virtuous behaviour occurs with the impartial spectator in mind. The man "who governs his whole behaviour and conduct according to those restrained and corrected emotions […] is alone the real man of virtue, the only real and proper object of love, respect, and admiration" (TMS VII.ii.18). Third, sympathy is a prerequisite to virtuous behaviour: "The man of the most perfect virtue […] is he who joins, to the most perfect command of his own original and selfish feelings, the most exquisite sensibility both to the original and sympathetic feelings of others" (TMS III.3.35). Fourth, self-command is the virtue from which all other virtues flow. In short, virtue consists of thousands of individual steps and decisions willed by the dictates of the impartial spectator and sympathy.

In Smith's time, there was a view that virtue was a matter of popular opinion. Today, that view might even be a majority view. However, it was not Smith's view. In a letter dated 10 October 1759 to Gilbert Elliot, who thought that the TMS treated virtue in an altogether too subjective manner, Smith writes, "I would beg of you to read what I say upon Mandeville's system, and then consider whether upon the whole I do not make virtue sufficiently independent of popular opinion" (CAS, 49).

In TMS, Smith reserves his greatest criticism of alternative theories of morality for Mandeville's *Fable of the Bees.* He writes: "There is*,* however*,* another system which seems to take away altogether the distinction between vice and virtue, and of which the tendency is, upon that account*,* wholly pernicious: I mean the system of Dr. Mandeville" (TMS VII.ii.4.6). Smith was at pains to show that there is an objective distinction between vice and virtue, that virtue is something real, so to say, and not just a deceitful manner of speaking as Mandeville had portrayed it.

Smith's interest in virtue is not with the characterisation of a person or a person's character but with the characterisation of an act. He discusses this in the section on

Aristotle's systems, where he observes "that virtue may be considered as the quality of an action, or the quality of a person" (TMS VII.ii.1.13). He continues: "Considered as the quality of an action, it consists, even according to Aristotle, in the reasonable moderation of the affection from which the action proceeds, whether this disposition be habitual to the person or not. Considered as the quality of a person, it consists in the habit of this reasonable moderation, in its having become the customary and usual disposition of the mind" (TMS VII.ii.1.13).

Just as virtue is a quality of an action, so its opposite is vice as a quality of an action. Virtue and vice are latent in every individual, and they need to be exercised by the individual to become what they are, virtuous or vicious acts. A child possessing the virtue of obedience to the parent still requires the parent's commands to exercise this virtue. At the heart of every virtuous or defective act is a choice, an act of the will. "Great merit in the practice of any virtue presupposes that there has been temptation to the contrary and that the temptation has been overcome; that is to say, it presupposes self-command" (Raphael and Macfie (1976) 1982, 6). A repeatedly renewed act forms the habit, and in this manner, virtue can be built or strengthened. Virtues become weak if not strengthened and fortified by overcoming opposite temptations. They require the occasions to be exercised. Naturally, the same applies to vice, which is strengthened by habit.

Smith's decision to identify virtue (or vice) not in the person but in the person's act deflects the question of nature away from human nature to the nature of the individual act. It is empirically more fecund. An act is in its existence discrete as opposed to continuous. Each act is separate and apart from every other act. In contrast, the person may be virtuous and continue to be so. The virtue of the person, being continuous in existence, has no identifiable beginning or end. However, the act of the will, the self-command or deceit committed is identifiable as either virtuous or defective. Criminals are convicted of an act of crime, not of a character.

Most human acts, however, are neither virtuous nor defective. These third kinds of acts are morally neutral and belong to the category of actions that may be approved but attract neither merit nor demerit. Their nature is mere *propriety*, a term that signifies proper action. Smith exemplifies these proper acts by the example of eating food when we are hungry:

> There is, in this respect, a considerable difference between virtue and mere propriety; between those qualities and actions which deserve to be admired and celebrated, and those which simply deserve to be approved of. Upon many occasions, to act with the most perfect propriety, requires no more than that common and ordinary degree of sensibility or self-command which the most worthless of mankind are possest of, and sometimes even that degree is not necessary. Thus, to give a very low instance, to eat when we are hungry, is certainly, upon ordinary occasions, perfectly right and proper, and cannot miss being approved of as such by every body. Nothing, however, could be more absurd than to say it was virtuous (TMS I.i.5.7).

In Smith's view, some ancient philosophers, including Plato, Aristotle, and Zeno, confused propriety with virtue. He argues that "though propriety is an essential ingredient in every virtuous action, it is not always the sole ingredient" (TMS VII.ii.1.50).

A neutral act can easily be turned into a defective or virtuous act. Given Smith's example of eating, what if someone eats when not hungry, or overeats? Gluttony is one

of the biggest problems in modern advanced economies, resulting in a massive disease burden. Since there is a name for it, this type of eating and drinking falls outside proper actions into the defective kind of action. While its etymology is rooted in matters of the throat, *gluttony* is now used to refer to other excessive behaviours, such as a gluttonous desire for money. On the other hand, abstaining from food or drink may be considered virtuous. In some religions, fasting at certain times will be considered virtuous.

Smith considered the great achievement of his TMS to consist of identifying the system of sympathy. It overcomes the arguments of those who consider self-love the motivation for all actions and the general standard of judgment of actions. The self-love paradigm does not distinguish between different kinds of acts. All acts are merely self-interested, though they may be classified ex-post depending on their effects. Smith's achievement is to show empirically that there is an elaborate ex-ante system at work in our judgement of acts and our conduct, even accompanied by "delicacy of sentiment and an acuteness of understanding" (TMS I.i.5.6).

The system of sympathy, deploying the three powers of the mind (will, intellect and memory), is such that we, as operating individuals, can easily determine – if we are honest to ourselves[2] – whether we act in a virtuous or defective manner, or when an act is neutral/proper. Only in the context of an ex-ante system does the ideal have relevance. I mean here not the ideal impartial spectator, per se, but the ideal of our conduct, guided by the system of sympathy. The ideal is to eliminate all defective acts and permit oneself only proper and virtuous acts. If the ideal is defined as the absence of a certain kind of act, then such an ideal presupposes the realism of different kinds of acts. Systems such as that of Mandeville deny the reality of such distinctions and accordingly have no space for ideals thus defined. Mere mortal beings may not achieve the ideal. However, we can ascertain how far we are short of the ideal by "these explanations of our moral personality in terms of empirical features of the mind" (Haakonssen 2002, xvi). The ideal of zero defective acts is represented in diagram 1 below at point 0 on the left vertical 0V axis.

Haakonssen argues that Smith "[i]n tracing law, politics and economy to their basis in the operations of the human mind, Smith was in effect suggesting that these moral institutions are natural to humanity" (2002, xi). Suppose the human mind is the basis for these institutions. In that case, one may explore the connections between institutions and the operations of the human mind, particularly the system of sympathy. So far, this article has explored Smith's real distinction between vice and virtue as qualities of acts. Following Evensky's interpretation of Smith's ideal liberal society that "would be inhabited by such perfectly virtuous beings" (2005a, 118), societies can be ordered from an imperfect society to an ideal one.

The imperfect society with only neutral or defective acts, with zero virtuous acts, is depicted at point V on the 0 V axis. The ideal society is depicted at point 0 on the same axis. The quality of institutions will be discussed in the next section before connecting

[2] In chapter 4 of Part III in the TMS, Smith argues that we may be prone in our judgement of our own conduct "to make a report very different from what the real circumstances of the case are capable of authorising" (TMS III.4.1). It is for this reason that we develop and rely upon general rules of conduct, which "are of great use in correcting the misrepresentations of self-love" (TMS III.4.12).

this aspect with the quality of acts via Smith's distinction between natural and market price and productive and unproductive labour.

8. Plunder and Classical Liberalism

The distinction between production and plunder, or between productive and predatory activities, is at the heart of the emergence of classical liberalism. Throughout history, individuals and peoples have been subject to plunder and atrocities. As Europe grew more affluent in the Middle Ages and Renaissance, forms of plunder nonetheless survived. Plunder and predatory activities hinder productive activities and are pernicious to economic progress. Classical liberalism emerged as an answer to the threat posed by predatory activities to economic progress. This is the "cosmic reading" of Mittermaier, who says that "in the very long line of thought of an emerging classical liberalism, in which Adam Smith was quite a latecomer, the ancient unsavoury art [of living at the expense of others, of getting others to do the dirty work for you] inspired a utopian vision of a market economy" (2019, 143). The various freedoms proposed by classical liberalism enshrine freedom from predatory activities so that individuals can get on with being productive.

Nonetheless, plunder and predatory activities continue to thrive to the present day. The more varied and complex productive activities have become, the more varied and insidious the predatory manners are. Large-scale financial crises, corporate collapses and state theft, all driven by avarice and greed and destroying the livelihoods of multitudes, depict the seriousness of the matter. "In our day of huge corporations, massive capital investments and large-scale unemployment […] [t]he difficulties of producing something on individual initiative are now so great that people find it easier to become political predators, to seek a share of whatever rent there is through political action, and thereby, without intending it, bring about a nonsensical allocation of resources" (Mittermaier 2019, 143).

Economics is ill-equipped to deal with the issues and even recognise an issue. National income accounts aggregate income into one value irrespective of that income's provenance (productive or predatory activities). National product accounts entrench the pattern, assuming that if someone or some entity has earned the income, it must have produced an output of equivalent value. However, according to national statistics, even cybercriminals working for registered enterprises earn an income and are deemed economically productive. Therefore, even predatory activities and plunder are recorded as productive outputs deserving an equivalent income. The distinction between production and predation has been eliminated.

Adam Smith considered the distinction between productive and predatory activities to be crucial for a correct understanding of the nature and causes of the wealth of a nation, finding fault in many of the business and state practices evident in Britain and elsewhere. The connotations of production and predation line up with those of the distinction between virtue and vice. Predatory activities constitute vice, and productive activities are virtuous. Smith's two books – the WN and the TMS – echo each other in this regard.

The view defended here on the relationship between the TMS and the WN is that they do not contradict their assumptions about human nature. The virtue from which all virtues flow is that of self-command. The human will can direct us towards virtuous or defective actions, though most of our actions are just neutral in a moral sense. The consequences of choices for virtuous or defective acts play themselves out at a personal level but also at an economy-wide level. It is with these latter that the WN concerns itself.

Smith argued that society's prosperity rested largely on business owners' initiative. The issue was stopping such individuals' initiative from turning into defective acts. The solution, he thought, lay in the common law: "Every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest his own way […]" (Smith [1776] 1952, 300). The sovereign is not burdened with "the duty of […] directing [industry] towards the employments most suitable to the interest of the society. According to the system of natural liberty, the sovereign has only three duties to attend to" (*ibid.*).

The problem, Smith realised, was that the sovereign or the state frequently did not restrict itself to those three duties but very often initiated steps to encourage or facilitate defective acts by the business owners or the state itself. The system of natural liberty was not something that existed; it was more of an ideal. The reality was different. As summarised by Mittermaier, Smith's view is that the government "is responsible for a firm administration of justice but frequently administers the predatory moves which merchants and manufacturers make on their countrymen" (2020, 66). Rather than citing various passages in the WN, illustrating Smith's displeasure with the business and government practices prevalent, it may suffice simply to quote his summary. In a letter dated 26 October 1780, he writes that the WN was a "very violent attack […] upon the whole commercial system of Great Britain" (CAS, 251). The result was that "Smith freely intermingled his prescriptions of market order with the descriptions of institutions which make up the bulk of the book" (Mittermaier 2020, 22).

The general equilibrium model of textbook economics assumes that all economic activities are productive and that predatory activities are absent. These are also the assumptions in Smith's chapter 7 of Book I of the WN, if only implicitly. In a realist political economy, the absence of plunder and predation in an economy is not an assumption but an ideal. Mittermaier summarises Smith as having "a vision of an ideal market order which, like other ideals, and together with other ideals, one has to strive to realise as far as one can" (2020, 21). The ideal institutional setup is one where the predatory activities are zero, at point P on the 1P axis in diagram 1, which will be elaborated on in the next section.

9. Realist Model

This section combines the above interpretations of TMS and the WN in diagrammatic form. Its underlying assumption is that the moral calibre of the individuals in a society affects the magnitude of that society's productive output and predatory activities. The moral calibre also affects the institutional framework, determining the degree to which it comes close to Smith's ideal of natural liberty. The implied causation also works the

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other way. Institutions that facilitate or encourage predatory activities affect not only productive output but also the overall morale and the ethical standard of society.

9.1 Virtue and Vice; Production and Predation

Diagram 1 depicts two vertical axes, 0V and 1P. Along the 0V axis is measured the proportion of acts that are either virtuous or defective. Neutral acts are ignored in this analysis. Acts are discrete entities, and at each point of an act, the operating individual knows, by what Smith has called the system of sympathy, whether an act is proper, defective, or virtuous. Individuals can self-report on the proportion of virtuous and defective acts. For instance, something like this establishes the world happiness index (https://worldhappiness.report/), which is also based on self-reporting information.

At A on the 0V axis, the virtuous acts amount to VA, and the defective acts are 0A; there is a higher proportion of virtuous acts than defective ones. The inverse is the case for K on the 0V axis. Non-neutral acts have either virtue or defect. The act of eating food tends to be neutral. However, overeating is defective, while restricting food intake for the benefit of others or for religious or even health reasons is virtuous. However, overdoing fasting is defective and may lead to death.

1P measures the degree to which the institutional framework of an economy favours predatory activity over productivity. The measures are empirical, for instance, transparency international and the fragile state index (https://fragilestatesindex.org/).

9.2 Productive and Unproductive Labour

Besides the distinction between vice and virtue and productive and predatory activities, Smith made further distinctions between productive and unproductive labour. The labour expended in services is considered unproductive. Productive labour feeds into the virtuous cycle of division of labour, surplus output and capital accumulation. Smith commences chapter 3 of book 2 in the WN as follows: “There is one sort of labour which adds to the value of the subject upon which it is bestowed: there is another which has no such effect. As it produces a value, the former may be called productive; the latter, unproductive labour” (WN II.iii.1).

This may appear to be a distinction without significance to the neoclassical mind. According to marginal productivity distribution theory, any labour that attracts an income is deemed productive. However, one can consider transaction cost economics in this regard. Wallis and North (1986) set out to measure the transaction sector in the US economy. They distinguish between the transformation and the transaction sector. Much of the transaction sector is about protecting property rights. Activities necessary to protect property rights include policing, litigating, patrolling, securing, defence, locking, *etc.* In a society where there are never acts of theft, bodily harm, negligence would largely do away with all these activities. In Smith’s terminology, they constitute unproductive labour. There is, therefore, a correlation between the two ratios of virtuous/defective acts, on the one hand, and productive/unproductive labour. Unproductive labour is not limited to just the protection of property. There are many other ex-

amples of unproductive labour in the sense that Smith had in mind, such as labour employed to satisfy our vanity, boastfulness, and many other desires/acts that are void of virtue.

The conceptual correlation between the quality of acts, on the one hand, and the texture of labour, on the other hand, is represented by line V1. VA constitutes a greater quality of acts than VK. Accordingly, VK is associated with a lower texture of labour at k than the texture of labour associated with VA.

9.3 Natural Price and Market Price

The fourth of Smith's distinctions introduced here is between market and natural prices. The natural price is the sum of input prices if the input markets are characterised by natural liberty. The natural price is "the lowest which the sellers can commonly afford to take and at the same time continue their business" (WN I.vii.27). Market prices may deviate from natural prices because of short-run supply and demand factors. More importantly, they deviate from each other if natural liberty is absent in the output market and (or) any of the input markets. "The price of monopoly is upon every occasion the highest which can be got. The natural price, or the price of free competition, on the contrary, is the lowest which can be taken […]" (WN I.vii.27).

The divergence between the market price and the natural price is a measure – PV in the diagram – referred to as the character of prices. A movement from P to V on the PV axis records increasing divergence of the market price from the natural price. P on the PV axis represents the situation where there is no divergence, where market prices equal the natural prices and thus represent the highest character of prices. "This […] would be the case where there was perfect liberty" (WN I.vii.30). P on PV also coincides with P on 1P, representing the ideal where there are no predatory activities, and all productive activities are rewarded with their natural price.

There is probably a positive correlation between the character of prices, on the one hand, and the quality of the institutional structure. The P0 line represents this. In low-quality institutional settings where plunder can flourish, market prices will likely deviate substantially from prices obtained under the ideal situation of natural liberty. Smith made related comments, observing that in poor countries, profits are higher than in wealthy countries.[3] 0 on P0 illustrates the end of the price system; prices cannot be charged because productive activities have ceased.

There is probably also a positive correlation between the character of prices and the texture of labour. Smith, for instance, lamented the system of primogeniture, which was then pervasive in England. First, the owner of large estates is little concerned with efficiency and is unlikely to invest in land productivity. "A merchant is accustomed to employ his money chiefly in profitable projects; whereas a mere country gentleman is accustomed to employ chiefly in expense" (WN III.iv.3). Given the concentration of land holdings in a few hands, prices will be above natural prices for the

[3] But the rate of profit does not, like rent and wages, rise with the prosperity and fall with the declension of the society. On the contrary, it is naturally low in rich and high in poor countries, and it is always highest in the countries which are going fastest to ruin.

product. On the other hand, the owner might have a large complement of menial servants, contributing to the barren texture of labour. At 0K proportion of defective acts, k' measures the barrenness of labour and l' is the indicator for the character of prices, recording a large deviation of the market price from the natural price. Associated with l' is an institutional framework at L that is permissive regarding plunder.

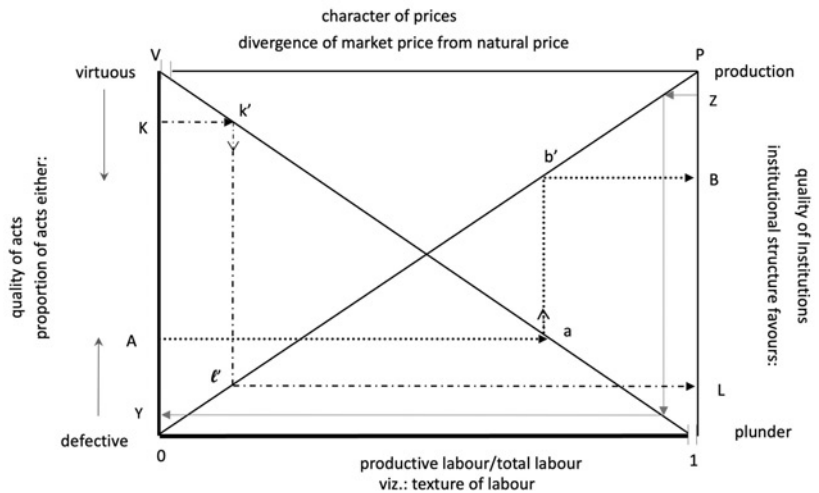

Figure 1: Moral-Economic Correlations: A Smithian Model
Source: Adapted from and inspired by Witztum 2016, 534.

10. An Application: Index of Moral Sentiments and Political Economy

The application of this model lies in identifying empirically where one is situated on each of the four measures or axes and monitoring how they evolve with each other. This can be done for a country or an organisation. An index can be developed to portray relative situations across time, countries, or organisations, with markers suggesting tendencies closer to or further away from the ideal combination represented at or close to Z and Y with a *stable* tendency.

The connections drawn in the diagram are meant to be empirical, not logical. Thus, the straight diagonal lines 1V and P0 serve a heuristic function, not a logical function. The diagram is not an exercise in rationalism but an exercise in realism. The actual correlation between quality of acts and texture of employment may not be a straight line such as the diagonal 1V. The diagonal lines are heuristic devices that combine the ex-ante and ex-post facts.

The measures portrayed on the two horizontal axes are based on records of past events. Market prices charged, and total expenditure on labour are ex-post facts. They are choices made against the backdrop of the institutional framework and the in-

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clination towards virtue or vice. The institutional framework consists of structures or guides to action that form the ex-ante facts against which production and pricing choices are made. An individual's ethical predisposition guides choices in the ex-ante order of facts. The ex-ante facts are more enduring than ex-post choices, but ex-ante facts also change over time.

Smith's concern was for ex-ante facts. He found fault with "the whole commercial system of Great Britain" in the WN (CAS, 251). He wished it would change in the direction of a system based on natural liberty, shifting the quality of institutions from L to B on the 1P axis. By all accounts, the British Parliament acted on Smith's ideas in the 20 years after the publication of the WN. (The enthusiasm for reform waned, however, with the growing influence of Malthus's pessimism.)

Against a more liberal system, allowing for competition and freedom of initiative, relative market prices would be closer to the natural price, providing for a better allocation of resources. The experience of increased globalisation provides evidence that within a free trade environment, greater competition leads to a lowering of market prices, reducing the divergence between the natural price and the market price. Naturally, enterprises prefer to bypass the market rather than compete on the market, depending on strong brand awareness to create a brand monopoly that can maintain a market price significantly above the natural price.

A situation close to the ideal is found at Z on 1P, where the institutional set-up strongly supports productive activities and discourages predatory activities. The market price is close to the natural price. Very little unproductive labour, associated with Y on the 0 V axis, indicates a close-to-ideal situation with nearly no defective acts. However, should the actual proportion of defective to virtuous acts be closer to A, that would put pressure on the institutional set-up, eroding some of the quality of the institutional set-up and moving it to B on the 1P axis.

Sen said that the "trouble with reading too much into … [Smith's] butcher-brewer-baker example is […] that it downplays the function of *institutions* that sustain and promote economic activities" (1995, his italics). In the proposed index, both the institutional set-up and the personal moral sentiments are given their due weight. "If [Smith's] ideal is to be more nearly approximated, the power of government must be continuously shifting from external institutional government to internal ethical government of individual citizens" (Evensky 2005b, 202). The model presented here, and the proposed index, is designed to track the dynamic of this ideal by means of ex-ante and ex-post facts.

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