

## Hayek, Rawls, and Schmoller Reconciled? Justice, Institutions and the Invisible Hand

By Richard Sturm\*

### Abstract

According to Schmoller, the key question about economic justice is: “How does it happen that economic transactions and social phenomena so often bring forth a favorable or adverse criticism which asserts that this is just, that unjust?” Schmoller’s question is answered in a way which makes sense of justice as an ingredient of modern institutional development. The argument is based on a framework of four conditions, allowing for the comparison of theories of social justice including Rawls and Schmoller with (1) Hayekian arguments sharply critical of social justice and (2) models conceptualizing the economic sphere as free from controversial distributive claims.

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### 1. Introduction

In his essay on “The Idea of Justice in Political Economy,” Gustav Schmoller takes issue with the “conception which sees in the difference between rich and poor only an occurrence of nature” (1894 [1881], 18). He argues that distribution – though mediated by the invisible hand of the market (“supply and demand”) – is ultimately *not* governed by “natural phenomena.” Distributive patterns are driven by prevailing institutions. Those institutions are not the product of blind forces, but rather, as Schmoller emphasizes, a historically contingent product “of human feelings and thought, of human actions, human customs and human laws” (*ibid.*, 22). According to Schmoller, this insight provides a basis for answering what he thinks is the key question with regard to the role of justice: “How does it happen that economic transactions and social phenomena so often bring forth a favorable or adverse criticism which asserts that this is just, that unjust” (*ibid.*, 3)?

Reconsidered in the light of more than a century of controversial discussion in social and economic theory, Schmoller’s question is aptly stated. But can this

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\* Institute of Public Economics, University of Graz, Universitaetsstr. 15, 8010 Graz, Austria. The author can be reached at richard.sturm@uni-graz.at.

question be answered in a way which makes sense of justice as an ingredient of modern institutional development? In the present paper, I will present arguments supporting an affirmative answer. However, evaluating these arguments requires taking into consideration arguments which are sharply critical of social justice (culminating in Hayek's verdict of "the mirage of social justice") as well as influential currents in economics construing the economic sphere as essentially free from controversial distributive claims.

Moreover, I will discuss Schmoller's reasoning in the context of two complementary strands of theory, which both refer to "social justice" (or some semantic substitute) as a conception with definite meaning. Schmoller's main concerns are common to those strands: (social) justice is conceptually relevant for the discussion of modern institutions, and it is the programmatic pivot of a social policy which neither amounts to technocratic redistribution nor to static embeddedness of markets.<sup>1</sup> The first of those strands approaches justice as a social phenomenon, primarily aiming at explaining its development and its function in terms of social/economic theory. It includes a tradition from David Hume (1739/40 and 1777) to Ken Binmore (2005) as well as contemporary scholars such as Peter Corning (2011), who attempts to explain "the pursuit of social justice" by utilizing insights from game theory, evolutionary and behavioral theory. Moreover, it includes theorists invoking a more organic conception of society, such as those who coined the notion of *social justice* in English language, among them Harvard economist Thomas Nixon Carver (1915), as well as an influential tradition of Catholic Social Thought inaugurated by Luigi Taparelli (1793–1862) and Heinrich Pesch (1854–1926).

The second strand stresses "social justice" as a comprehensive normative concept, which finds its motivation in the complex multi-level structure of modern societies. Its main thrust is most succinctly summarized by the legal philosopher Peter Koller (2001a; 2001b; 2016), who defines "social justice" as the sum of all justice-related requirements applying to the various levels of the basic institutional order of society. Social justice is thus considered as an overarching concept, including terms like "distributive justice," "commutative justice," "political justice" and "corrective justice."

Section 2 will discuss those two strands, stressing in particular works and thinkers who attempt to merge them. This includes two political philosophers who systematically and explicitly address the role of social science: David Miller (1999) and John Rawls (1971). Section 3 highlights some specificities of Schmoller's discussion of justice and combines this with making explicit crucial conditions of Rawls's framework not commonly stressed in the literature. Thereafter, I shift attention to two theoretical conceptions of the market

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<sup>1</sup> I do not discuss thinkers *mainly* concerned with ethically appropriate limits of price-mediated exchange (see e.g. Sandel (2013)).

economy, associated with Friedrich Hayek (section 4) and in respect to Leon Walras and Abba Lerner (section 5). If considered in isolation, both conceptions do not directly contribute much to the understanding of social justice in the socio-economic development of “Great Societies.” For Hayek *social* justice is a mirage. For Walras-Lerner it is anathema. The main reason for this shift of focus is not that both of these views are hugely influential and criticizing them may hence be of some interest. They are of interest for a different reason: elaborating both views and their crucial assumptions enables us to consider the contours of worlds in which “social justice” indeed has no specific meaning and may degenerate into misleading political rhetoric. Both views pose specific and important challenges. Those challenges are associated with the demonstration of conditions which would (if they held in the real world) render social justice obsolete: either it may become obsolete because there is no way to implement justice-enhancing reforms, or it is obsolete because all issues involving justice can be decomposed – the distributive aspect can be isolated and dealt with as if it were a simple “cake” distribution problem. An overarching concept such as social justice is not useful at all. It is contended here that properly addressing those challenges is important not only for disambiguating the concept of “social justice,” but also for clarifying its scope and its premises.

## 2. Justice in Great Societies: Why Social Justice Matters<sup>2</sup>

Friedrich von Hayek (1976) not only called the idea of “social justice” a mirage, but supplied an impressive list<sup>3</sup> of characterizations leaving no doubt that he considered it a hollow formula *and* a dangerous superstition. It is not unlikely that a comprehensive empirical study of the actual use of “social justice” as a political slogan would to some extent support Hayek’s dismissive stance. Indeed, the meaning of “social justice” often remains vague in public discourses. In other cases, it is used interchangeably as a synonym for the time-honored concept of distributive justice. The latter applies to a British tradition of utilitarianism with John Stuart Mill and Henry Sidgwick as main protagonists (see Miller 1999, 3 and 269 n. 5). Both classes of cases will not be discussed further here.

However, there are also respectable intellectual traditions where the concept of social justice indeed has a specific meaning: scholars who prominently use

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<sup>2</sup> See Barry (2005) for a book with this title, addressing this question in a normative and political perspective.

<sup>3</sup> See Lister (2013, 410) for a comprehensive summary of this list, which may be complemented by Hayek’s remarkable statement: “The greatest service I can still render to my fellow men would be that I could make the speakers and writers among them thoroughly ashamed ever again to employ the term ‘social justice’” (1976, 97).

the term “social justice” wish to emphasize specificities of the complex multi-level institutional settings of “Great Societies” (a term used by Adam Smith and Hayek, but also by Taparelli), leading to a more comprehensive view of the demands of justice. Beginning in the 1840s, scholars with different backgrounds thus used the notion of “social justice,” thereby expressing two related kinds of concerns. One of those concerns is motivated by the idea that the complexity of Great Societies requires an overarching integrated normative framework for balancing justice-related claims. The second emphasizes the priority of (what is considered as) up-to-date socio-economic theory for studying the role of justice in modern society. Theoretical work on justice needs to be supported by some kind of socio-economic analysis explaining the functions of justice within the actual working of social institutions and mechanisms. There is at least one aspect which is common to both concerns: they stress the interest in normative frameworks related to a specifically relevant class of societal contexts (Great Societies).<sup>4</sup>

This certainly is true for Luigi Taparelli D’Azeglio, S. J. Taparelli (1840) is credited with having first introduced the term social justice (*giustizia sociale*) (see Hayek 1976, 176; Solari and Corrado 2009). An eclectic thinker in a Catholic, scholastic tradition of natural law, Taparelli was primarily concerned with normative issues when introducing *giustizia sociale*: he explicitly stated that the factual conditions of emerging industrial society requires developing normative concepts beyond commutative justice (see Solari 2007; Solari and Corrado 2009). However, it is noteworthy that this concern was addressed within a theoretical program which was considered an alternative social theory by its author. It was developed to correct the one-sidedness of then dominant “liberalistic” currents of Political Economy. In many respects, Taparelli (1840) indeed posits a social theory with specific metaphysical assumptions about the nature of man – but “supported by facts” – as the second part of its title indicates. A key outcome of this theory is a kind of multi-level system of governance in Great Societies including the principle of subsidiarity. In this context, social justice on the one hand requires a social arrangement such that all of its parts and all individual members get everything they need for exercising their functions. On the other hand it demands from the individual to bear her due share of the burdens associated with the flourishing of the commonwealth. This

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<sup>4</sup> To be sure, important currents of theory which stressed the development of normative frameworks specifically adapted to the institutions and mechanisms of market societies and did not use the term “social justice.” Indeed, the word “social justice” is absent from David Hume’s (1739/40) pioneering explanation of justice as an “artificial virtue” playing a key role in a carefully defined socio-economic context relevant for market societies. It is also absent from Adam Smith’s important references to the delicate balancing of justice-related claims and issues of distribution in *The Wealth of Nations* (1776, I. viii. 36 f. and V. i.f. 48 ff.), not least regarding the extent to which tax-financed public expenses are compatible with justice.

understanding of social justice was further developed in the German tradition of Catholic Social Thought by Heinrich Pesch, Gustav Gundlach and Oswald von Nell-Breuning and became a central concept in the papal encyclical *Quadragesimo Anno* (1931). In this view, social justice is a pivotal condition for a prosperous social economy and the flourishing of its members.

Notice that the emphasis on such interdependencies between individual and collective flourishing is not unique to Catholic Social Thought. Organic views of society support similar arguments in the writings of scholars who coined the notion of social justice in the Anglo-Saxon world towards the beginning of the 20<sup>th</sup> century. The latter include Westel W. Willoughby (1900), a political theorist from Johns Hopkins University. As pointed out by Miller (1999, 4), Willoughby was influenced by the British idealist school of the social-liberal philosopher Thomas Hill Green. Without using the term “social justice,” Green had linked justice to the idea that a properly adjusted system of private property would benefit all, in particular the least well-off. As further protagonists, the British social philosopher L. T. Hobhouse and the Harvard economist Thomas Carver should be mentioned. Carver complements his organic view by suggesting social justice as a property relevant for evolutionary selection: justice makes a group strong and progressive, while injustice is a “system of adjusting conflicting interests which makes a nation weak and retrogressive” (1915, 30). At this point it should be noted that the diagnosis of an interdependence between individual and collective flourishing was also developed by Adam Smith who is not normally seen as a protagonist of organic economic thinking: he states that “no society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable. It is but equity besides that those who feed, clothe and lodge the whole body of people, should have such share of the produce ... as to be themselves tolerably well fed, clothed, and lodged” (1776, I.8.36f). In Smith’s theory, this is certainly not an ontological truth (as it may be true for some organic theories), but is established as a result of certain macro- and microeconomic conditions of what Smith calls the “progressive state” of society. Justice-relevant interdependences between the individual and the collective level can thus be brought to the fore in different types of social theory.

Now consider scholars employing the notion of social justice from the perspective of normative theory. A transparent account is developed in Peter Koller’s (2001a; 2001b; 2016) conceptual analysis of social justice. Koller’s definition of social justice explicitly refers to different spheres of social interactions and concomitant institutions, which are the locus of the different dimensions of justice. This includes “distributive justice,” “commutative justice,” “political justice” and “corrective justice.” Assuming important interdependences between those spheres, a suitably intergrated concept of social justice does make sense. Given such interdependences, considering the different dimensions (such as distributive and commutative justice) in isolation may be the root of prob-

lems. For the political philosopher David Miller (1999), social justice is also a compound concept involving a balance of different kinds of claims, including need, desert, and equality, which again correspond to different domains of social interactions. Miller is very explicit in stressing the indispensable role of social sciences (including social psychology and empirical research on justice) for any discussion of social justice; indeed, the third chapter of his book is devoted to the demonstration that “social scientific and philosophical studies of justice are necessarily interdependent” (1999, 43). By way of conclusion, Miller sketches some arguments referring to the different prospects of various dimensions of social justice (need, desert, equality) under 21<sup>st</sup> century conditions such as “globalization.” It is contended that globalization may affect the socio-economic premises of the respective dimensions differently.

The most important thinker using “social justice” as a definite concept is John Rawls. Even though Rawls’s perspective is fundamentally normative, *A Theory of Justice* (1971) is contextually specific in relying on social theory from the beginning: it aims at specific relevance for certain types of societies. Their properties are carefully designed to include contemporary market societies. The pertinent design is based on assumptions which cannot be assessed without socio-economic theory and empirical social sciences. Rawls’s multi-faceted edifice thus includes discussions related to economics and social psychology, invoking problems of social coordination, efficiency, and stability (see Barry 1995). Discussions of reciprocity and the sense of justice and envy play a notable role.<sup>5</sup> The key part of the architecture arranging those socio-economic aspects is borrowed from the theoretical apparatus introduced by Hume. This includes the (empirical) “circumstances of justice” characterized by moderate scarcity and limited generosity as well as “the logical importance of general rules.” This motivates Rawls to state that “the conception of justice which I set out is perhaps closer to Hume’s view than to any other” (1999, 240 n. 4). On the basis of those “circumstances of justice,” Rawls (1971, 110) defines social justice as the first virtue of social institutions.<sup>6</sup>

All this leads to a framework where social justice is *not* equated with distributive justice. Distributive justice is relegated “to a subordinate place” (*ibid.*, 546) in the overall architecture. He is looking for a framework of justice which is *specifically apt* to function in the context of the evaluation of alternative institutional arrangements coordinating cooperative production and distributing its product in a stable fashion. Distributive criteria which are part of this eva-

<sup>5</sup> For a comprehensive account of Rawls’s moral psychology, see Baldwin (2008).

<sup>6</sup> Rawls’s institutionalism has been somewhat neglected in most currents of Post-Rawlsian literature, not least those which gained ground among economists. Social justice is thereby reduced to distributive justice. It seems that some of the issues addressed by Rawls by way of his multi-level institutionalism are transferred to the equality-of-what debate dominating the intellectual exchange between normative economics and Post-Rawlsian political philosophy in recent decades (see e.g. Sen 2009, part III).

lative framework may not (and, in general, will not) be best suitable in the context of other distributive problems, such as dividing an exogenously given cake, or choosing the amount of money you give to a charity. As stressed in “The Basic Structure as the Subject,” Rawls’s “principles of justice do not insist that the actual distribution reflect any observable pattern, say equality, or any measure computed from the distribution, such as a certain Gini coefficient” (1977, 164). Rawls’s theory even leads to the seemingly pragmatic (or minimalist) conclusion that “on many questions of social and economic policy we must fall back upon a notion of quasi-pure procedural justice” (1971, 201)<sup>7</sup> <sup>8</sup>, as well as to second-best considerations about “non-ideal theory” – to be applied in cases where a just social equilibrium seems to be out of reach.<sup>9</sup>

By way of conclusion of this section, let us note some common perspectives of the different strands of scholars using the notion of social justice with a definite meaning:

- (i) Protagonists of social justice are liberals, bourgeois progressives and moderate reformers, not advocates of socialist revolution. The market economy and the system of private property rights is considered as defensible, albeit in a qualified way. Its institutional framework is subject to change; it evolves with socio-economic conditions.
- (ii) The subject of social justice is the system of rules and institutions. Statements about social justice hence are not reducible to a one-dimensional metric, e.g. to a welfarist metric. As David Miller puts it, “social justice has to do with the means of obtaining welfare, not with welfare itself” (1999, 7).

Both (i) and (ii) are also valid for Schmolter. Some specificities of his theoretical edifice are now considered in greater detail.

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<sup>7</sup> Pure procedural justice must be distinguished from perfect procedural justice: suppose that justice is about the distribution of a given amount of scarce resources. In that case it makes sense to introduce an independent criterion of distributive justice (e.g. equality) yielding a specific distribution of resources. The mechanism implementing this distribution (e.g. “I cut, you choose”) would be characterized by *perfect* procedural justice. Rawls’s example for *imperfect* procedural justice is a court system, where it occasionally happens by mistake that the guilty are acquitted and the innocent jailed. A fair lottery is a case of *pure*, and social justice of *quasi-pure* (or defectively pure) procedural justice. In both cases we lack an independent criterion for just results (which is obvious in the lottery-case), while circumstantial complexities may cause a certain latitude of judgement in the case of social justice. See Bedau (1978, 173).

<sup>8</sup> Hugo Adam Bedau (1978, 172f) shows in more detail why a proper understanding of the “institutionalism” introduced in the *Theory of Justice* brings Rawls to the conclusion that “the best attainable scheme is one of imperfect procedural justice” (1971, 198).

<sup>9</sup> In situations of institutional change, non-ideal theory as well as the theory of second-best institutions may be especially relevant. For the latter, see Rodrik (2002).



### 3. Rawls After Schmoller: Schmoller Vindicated?

The impact of institutions on distributive patterns is described by Schmoller in a way comparable to Rawls's analogous account of the way in which the "basic institutional structure" influences individual prospects.<sup>10</sup> Specific weight is placed on an independent role of normative discussion. Distributive prospects and outcomes are subject to criticism: pertinent normative discussion is unavoidable and has to be taken into account as factual reality to the extent that institutions are (perceived as) human-made. Schmoller thinks that all this is unduly neglected by economists promoting dismissive views with regard to discussions of distributive justice. Those economists believe that so far as

mankind demands a just distribution of incomes, their ideas are in the main foolish; justice may at the most be demanded of the State when it intervenes directly; opposed as it is to free intercourse and the legitimate influence of fortune, this striving is wrong. 'Shall we,' we hear from this quarter, 'censure our God, that He so frequently interferes unjustly? Shall we prescribe to Him where His lightnings shall strike and where He shall permit the bullets to hit? Shall we quarrel with nature because she grants the delicious fruits of the south and an olympic existence to one race, while she banishes another to the reeking hovels of the arctic (Schmoller 1894, 18)?

By contrast, Schmoller concludes his reasoning on the distributive impact of economic institutions, which are a product of "human feelings, thought, and action" as follows: "And just this causes us to apply the standard of justice to their results, just this makes us inquire whether they and their effects are just or unjust. We do not require the distribution of incomes or wealth to be just absolutely; we do not require it of technical economic acts which do not concern others; but we do require the numerous economic acts which on the basis of barter and division of labor concern others and entire communities to be just" (*ibid.*, 22). While conceding that the "individual scholar who, in his researches, considers only forces, proportions, demand and supply, and endeavors to grasp them, may ignore the question whether the result be just ...", Schmoller insists that "as far as human action governs and influences the distribution of incomes, so far this action will create the psychological processes whose final result is the judgment which finds the distribution just or unjust; so far as blind extra-human causes interfere, reasonable reflection will demand that men should submit to them with resignation" (*ibid.*, 19). Hence normative discussion on distribution typically will have a theoretical rationale and at any rate will be factually

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<sup>10</sup> Schmoller writes: "If it is objected that demand and supply distribute incomes, we reply in the first instance: Are demand and supply blind powers independent of human influence? ... The prevailing rights of property, inheritance and contract form the centre of the institutions which govern the distribution of incomes. The individual causes and the chance of luck effect within the bounds of these institutions the little aberrations of personal destiny; the position of social classes in general is determined by the institutions" (1894, 20).



relevant: "... the popular mind will always repeat the question as long as it sees before it human actions" (*ibid.*, 18). In *Political Economy*, it would be silly to ignore factually occurring normative discussions, as they have real effects: it may be interesting to learn "what force, weight and influence this approving or disapproving judgment will exercise retroactively on the social and economic phenomena" (*ibid.*, 4).

Schmolter's reasoning on justice has a strong institutional focus with an idealist turn: "We demand today above all just economic institutions, i.e., we demand that the complexes of rules of morals and right which govern groups of men who live and work together should harmonize in their results with those ideal conceptions of justice which on the basis of our moral and religious conceptions are prevalent today, or which are gaining recognition" (*ibid.*, 35). The second part of this sentence indicates Schmolter's idealist heritage. Institutional development is related to the evolution of conceptions of justice, which in turn is associated with the (progressive) evolution of mental models. However, in the final part of the following passage referring to the historicity of justice, Schmolter points to functional dimensions closer to Hume's and Rawls's view of the empirical contingency of justice according to the circumstances of justice: "We do not acknowledge any one of these institutions to be above history, as having always existed or as necessarily everlasting. We test the result of every one of them, and ask of each: How did it originate, what conceptions of justice have generated it, what necessity exists for it today" (*ibid.*, 35)?<sup>11</sup>

The framing of those views is related to Schmolter's idealist psychology: progress with regard to justice-related aspects of predominant ethical views seems the key to overall progress and flourishing. It is in the non-material cultural spheres of religion and ethos (not technology and economy) where the potential of humanity in an emerging stage becomes visible first. Ideally, ethos and concomitant institutional arrangements are up to the cultural challenges (*Kulturaufgaben*), given the historical stage under consideration. In the present stage of civilization, public institutions (notably including the state) channel the forces unleashed in the market economy as a game played by individuals. They thus regulate the distribution of income. In that sense, the market economy is not a natural order. Market remunerations are not "natural," as they are influenced by human artefacts (institutions). Inspired by Hegelian thought with regard to wider historical horizons, Schmolter envisages a dialectic dynamism in the development of individuality co-evolving with an ever more just public order. Progress implies that social interdependencies are mediated with less and

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<sup>11</sup> Some passages from Schmolter may suggest that he is concerned with distributive justice only. However, his discussion of (i) norms and institutions as key influences with regard to distribution and (ii) of justice as a key coordinate of (factual) public criticism of social states and deliberate institutional change is in keeping with the main thrust of what theorists of social justice (as discussed in section 2) considered important.

less coercive and power-related means, as the actual state of affairs converges towards what everybody endorses as “just.” Bourgeois society with its characteristic norms, regulations and its vast scope of decentralized decision-making is just an intermediate stage in this process.

While some specificities regarding the status of justice within Schmoller’s theory are related to idealism and historicism, not everything he has to say about justice stands and falls with this historicism. Schmoller’s substantive claims seem to make some sense. However, the core of Schmoller’s views and of related reasoning on social justice may be challenged by considering two lines of argument which both have been developed in economics. Each of them makes available specific insights which are crucial for critically assessing the systematic role of justice in “Great Societies.” The first of those insights sharply focuses the destructive potential of inadequate normative standards, epitomized by Hayek’s (1976) slogan of *The Mirage of Social Justice*. The second insight draws on the potential analytical and practical benefits of keeping apart two different spheres of human interaction: a sphere of purely economic transactions, and a sphere where distributive problems are dealt with. For reasons explained later, I call this the Walras-Lerner view. Moreover, while those two strands of economic reasoning are highly useful for discussing qualifications of conceptions of social justice, both of them are based on sets of assumptions which are controversial, judged by standards of historical experience and current empirics. However, they may be congruent with some developments in modern societies which may render them more realistic.

Protagonists and antagonists of social justice may be discussed within a common framework made available by the premises of “institutionalism” à la Rawls: an institutionalist conception of social justices presupposes a society (A) of interdependent agents under conditions of moderate scarcity and limited generosity, which moreover is in a stage of technological development such that it amounts to (B) a cooperative venture for mutual advantage, mediated (C) by a system of norms/institutions demonstrably affecting the prospects of those agents in a systematic way. Last but not least, it (D) presupposes a collective agency (or a multi-level system of collective agencies) which is capable of deliberately changing the system of norms/institutions such that it improves according to the demands of social justice. (A)–(D) are either stressed or implied by Schmoller and the protagonists of social justice. Assumption (B) is phrased here in the well-known version coined by Rawls (1971) with an individualist social theory in the background. In organic social theories one instead would invoke some natural complementarity between the individual parts in a setting of specialisation and division of labour.

Here is the key message from what follows now: it is worthwhile to imagine worlds where one or more of these assumptions do *not* hold. Hence let us briefly discuss (A)–(D). Unless one believes that we may approach an economy blessed by affluence or constrained by resource bottlenecks, investigating (A) may seem

least interesting. As already explained by Hume (1777, III.i. 145 ff.), both absolute abundance and absolute shortage (food in a besieged city) are not conditions under which the sought concept of justice is useful. (B) invokes non-zero-sum interaction and the existence of a cooperative surplus. In contrast, a standard neoclassical world (where competitive remunerations of productive services exhaust the total value of the “cooperative” product) makes the case for “social justice” (not for distributive justice!) difficult, as will be argued in section 5. In addition to the trivial case of neutral norms/institutions, assumption (C) fails when norms/institutions somehow matter for individual prospects, but the effects are not patterned in a traceably systematic way; hence no class of agents has sufficient reasons for complaints. A further potential problem with (C) is related to the boundaries of the basic institutional structure (see Bedau 1978, 167–71).<sup>12</sup> (C) presupposes that the basic institutional structure can be clearly identified, with a constitutional level and political institutions (including tax-and-transfer systems, social policy institutions and so forth) as “core” elements. However, in addition to the core norms regarding property, exchange, and distribution, a great variety of informal norms, intermediate institutions, family structures and feedback between the various levels may affect outcomes; more recent developments in fields such as behavioural game theory allow for taking into account such feedback.<sup>13</sup> If such aspects are found to matter, the boundaries of the basic institutional structure may become fuzzy. The status of (C) then depends on whether this problem may reasonably be addressed by the multi-level framework, including pragmatic, but consistent ways for drawing the line, as suggested by Pogge (2000). Finally, there are several reasons why (D) might be problematic. One class of reasons is related to inherent problems of political decision-making, involving distortions and incentive-problems which make it possible that politics serves some special interests, but is not capable of improving the rule system according to the demands of social justice. A second class of reasons is illustrated by the fact that Rawls relates “social justice” to a political entity such as the nation state, including a clearly defined set of people, with some minimal agreement about the means and freedoms important for the plurality of ways in which a “good life” is conceivable in liberal societies. In contrast, consider the discussions about global justice where (D) may fail on those grounds: suppose that (A)–(C) can be shown to apply to the context of the global society (as is claimed by Abizadeh 2007). However, the prospects for emergence of global agencies capable of promoting social justice may be gloomy, as minimal agreement may be difficult to attain (cf. Rawls 1971, 457).

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<sup>12</sup> Further references include three articles consecutively published in *Philosophy and Public Affairs*: Cohen (1997), Murphy (1998), and Pogge (2000). This little debate is one of the few cases where Hugo Bedau’s paper “Social Justice and Social Institutions” (1978) receives due attention. See also Rawls’s “The Basic Structure as the Subject” (1977).

<sup>13</sup> See for instance Denzau and North (1994), Bowles (1998) and Bowles (2004).

With regard to challenges to (A)–(D), Hayek mainly disputes condition (C) and (D), while the thinking of many neoclassical economists is framed by standard textbook models where (B) and (C) do not play any role. Notice that (C) is clearly stressed by *classical* economics of the 19<sup>th</sup> century, which was much concerned with the distribution of the productive surplus among social classes. (Schmoller was aware of this and vividly emphasized C!) Neither Hayek nor neoclassical economics develop any deep principles which would preclude studying the relation between rule systems/social structures and prospects/outcomes of some classes of individuals. However, the status of this question is weaker than in classical economics and somehow in the shadow of the model of the market as game of skill and chance. In the following section, I will mainly deal with (D) which in itself is quite complex, as it does not only hinge upon whether one is more or less optimistic regarding the working of political mechanisms, but also the properties of spontaneous orders and invisible hand mechanisms. Section 5 deals with the neoclassical challenge which gives leverage to two lines of reasoning with quite different political implications, both of which tend to render social justice (in the understanding stressed in the present paper) obsolete.

#### 4. Spontaneous Order and the Game of Skill and Chance

Rawls's concept of justice addresses the evaluation of rule systems giving rise to the "basic social structure" of society. Viktor Vanberg (2006) and Andrew Lister (2013) discuss the extent to which the theoretical architectures of Hayek and Rawls are in fact similar, even though Rawls is the leading protagonist of social justice, while Hayek's antagonistic stance seems beyond any doubt. According to Lister, the differences between Hayek and Rawls at a basic conceptual level are small. Given Rawls's Humean roots mentioned above and Hume's influence on Hayek, this is not surprising. As stressed by Lister (*ibid.*, 410f), Hayek was to some extent aware of those similarities, stating that his differences with Rawls are "more verbal than substantial" (1976, xiii). One may add that this applies to Rawls's thought, but less to much of the literature in the wake of Rawls (1971), in which those Humean roots played no big role and social justice and distributive justice are often used as synonyms.

I also agree with Lister's diagnosis according to which the differences between Hayek and Rawls are mainly driven by "a set of empirical claims, particularly claims about feasibility" (2013, 431). However, this "set of empirical claims" is complex. Indeed, Hayek endorses a sophisticated combination of conjectures which is *prima facie* quite reasonable: Hayek is a moderate sceptic regarding the working of the political sector (the visible hand) and a moderate optimist with regard to the properties of the spontaneous order. Hayek's politi-

cal scepticism is moderate as he (like other Austrians such as Schumpeter) endorsed an intermediate position: he rejected overoptimistic views defended or implied by constructivist rationalism, but did not subscribe to the more pessimistic stance articulated by anti-enlightenment thought from Joseph de Maistre up to Carl Schmitt. He believed that evaluating political institutions according to the demands of justice does make sense, stating that there “unquestionably also exists a genuine problem of justice in connection with the deliberate design of political institutions, the problem to which Professor John Rawls has recently devoted an important book” (Hayek 1976, 100). Following Adam Smith, he thinks that we may reasonably aim at influencing the political sector such that attempts to use it as a tool for subverting justice for the sake of special interests are blocked.

Hayek’s moderate optimism does not imply that spontaneous orders or the invisible hand of the market are *always* optimal. However, scope for improvement by deliberate design is tightly limited. Let us first briefly discuss the invisible hand of the market, which also will play a role in section 5. For Hayek, the invisible hand of the market amounts to a game of skill and chance where the problem underlying condition C (see the final part of section 3) is of second-order (if any) importance. In any case, (C) is not found sufficiently important to motivate an adjustment of the rule system on the grounds of fairness. Two kinds of reason play a role here: (i) The adjustment of rules is a delicate task and impeding the function of the market as a discovery process must be carefully avoided; (ii) the market itself tends to be seen as a process eliminating (and *not* petrifying or even amplifying) the effects of social structure (based on class, race, or gender) on individual prospects/outcomes. However, the extent to which both (i) and (ii) are actually true is an empirical issue. On the one side, in a market with increasing returns and/or information asymmetries, it is less likely that the market as a game of skill and chance has this desirable property (e.g. increasing returns may amplify discriminatory effects). On the other side, information asymmetries are also the starting point for models where improving the fairness of rules increases market efficiency. This may widen the scope for reasonable reforms “improving” the rule system in order to attenuate unfair effects of “social structure.”

Hayek’s moderate optimism regarding systems of rules and institutions spontaneously grown in an evolutionary process is the basis of his dismissive stance vis-à-vis naïve constructivist reformism. Such institutions may contain the wisdom of generations in a non-obvious way. While one should take these arguments seriously, Hayek’s moderate optimism with regard to the foundational spontaneous order of civil society needs to be qualified. In the following, I will discuss this moderate optimism in the context of a more general analysis of institutions. Here is a sketchy account of the general architecture of such an analysis: institutions are understood as a response to the problems occasioned by the nature of social interdependences.

Given some minimal assumptions about individual purposes common to Rawls, Hayek, and other individualist theorists, those interdependencies are driven by properties of the environment: a description of the environment primarily includes the availability conditions of all kinds of scarce exhaustible and renewable resources, the availability and distribution of codifiable and non-codifiable knowledge, the properties of technologies, and climate conditions, among others. Ensuing patterns of interdependences are shaping concomitant strategic interaction situations. The structure of those problems can be described as strategic interaction problems in game-theoretic frameworks. It has implications for the status and scope of deliberate coordination and of designed institutions. Whether or not (1) some kind of deliberate design/improvement of rule systems, or (2) a political-constitutional level as part of the institutional framework, or (3) something like “social justice” has a role to play depends on the properties of strategic interaction problems. (Those properties define what for Hume and Rawls are the empirical “circumstances of justice.”)

Strategic interaction analysis allows one to assess the plausibility of different scenarios, relating them to various kinds of institutions which can be explained as responses to the interaction problems. For instance, the game structures of the underlying games may all allow individuals to spontaneously coordinate on “good” equilibria.<sup>14</sup> Suppose that all genuinely relevant strategic interaction problems have a unique equilibrium, which happens to be an equilibrium which is “good” for everybody – i.e. the pattern of individual outcomes in this equilibrium is such that nobody ever will have good reasons to think about ways and means to secure a better outcome (e.g. by way of collective action changing the rules of the game). Then (1)–(3) are simply redundant. Put another way, we are in a hyper-Hayekian world where all relevant games are invisible hand games, and there is simply no need and no place to introduce collective institutions mediating human interaction – not even justice in the Humean understanding would have a place.

However, some game structures imply social dilemma situations, where society is trapped in a sticky bad equilibrium. Let us hence change the assumptions about the kind of games which are relevant. A positive role for *design* is associated with the relevance and scope of interaction situations with a unique equilibrium which is “bad” for everybody (such as in typical public goods games), as we should expect unanimous support for a deliberate change of rules. A positive role for *justice* seems to be associated with the scope and relevance of situations with multiple equilibria. For sake of the argument, suppose a situation with three equilibria: the first equilibrium is stable, but not efficient or fair. A second equilibrium is stable and efficient, but not fair. For instance,

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<sup>14</sup> This may be discussed in different settings regarding the time horizon (repeated games) and with different equilibrium concepts, including those suggested by evolutionary game theory.



certain forms of segmentation/discrimination may be shown to be stable and efficient, but unfair responses to strategic interaction problems (see Bowles 2004, 244 ff. for some simple models). Finally, a third equilibrium is stable, efficient, and fair. At least three messages can be derived from such examples. First, the possible emergence of stable and efficient, but unfair equilibria (which embody some “wisdom,” but perhaps not enough) suggest that the moderate optimism with respect to the invisible hand needs to be carefully qualified. Second, in such cases “natural” justice may be discussed as a potential equilibrium selection device (see Binmore 2005). Third, such situations are more complex than those with a unique bad equilibrium, including several plausible ways of setting the scene for some deliberate institutional change and design (“institutional improvement”). Schmolter’s idealist psychology may provide a heuristic framing for thinking about how the development of mental models (see Denzau/North 1994) may play a role in an overall progressive development rendering justice increasingly important.

Reconstructed in the game-theoretic framework, Rawls’s “circumstances of justices” assume that strategic human interaction is composed of a mix of various types of games, including invisible hand games as well as a range of social dilemma and multiple equilibria games where the idea of collective improvement and the idea of justice may appear “natural” in the sense sketched above. Political thinkers such as Hobbes and Hume (1739/40, book III; 1777) assume a somewhat different mix of games, and discussed various ways by which a change of rules (“improvement”) may be brought about in societies with pertinent social dilemmas. The suggested schemes of improvement differ in particular with respect to the scope of design, but those differences again can be shown to hinge upon different assumptions on the kind of relevant games.<sup>15</sup>

Suppose that the mix of problems assumed in Rawls’s description of the circumstances of justice roughly corresponds with our empirical knowledge about resource availability, technologies etc., and that the pattern of games associated with that will not change in the foreseeable future. This leads us close to the concept of “justice as the first virtue of institution” à la Rawls. Moreover, in terms of the status of political reform it leads us to a position implying a wider scope for justice-oriented reforms compared to Hayek, while it still qualifies as Whiggish according to Binmore’s (2005, 186 ff.) classification: without much ado, it takes on board Hayek’s message regarding the complexity of society including the possibility that grown institutions entail more “wisdom” than is *prima facie* obvious. This is reflected by the fact that our protagonists of social justice tended to be cautious reformers.

Consider a further advantage of taking strategic interaction situations as points of departure: it becomes almost immediately clear why alternatives to

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<sup>15</sup> See Hardin (2007), for instance, for a comparison between Hobbes and Hume.



“the basic institutional structure” in defining the subject of justice are less useful. In strategic situations the outcome (for me and for the other players) does not only depend on my choices, but also on others’ choices. Hence individual-centred definitions of the subject of justice (individual acts, individual persons, the character of those persons as in virtue ethics) are problematic. It moreover becomes obvious why the distributive pattern (as considered by simple distributive justice) is problematic as subject of social justice, as it is detached from the interaction structure giving rise to an outcome. Hayek (1976) indeed should be read together with Rawls (1971 and 1977, 164), who argues that “whatever distributive shares result are fair” – referring to the outcome of what can be understood as a game played under fair background conditions. Rawls is no less clear than Hayek (1976, chapter 9) that political interference with the outcomes of fair games poses specific problems which cannot be properly addressed by a “justice czar,” a phrase used by David Schmidtz (2012). By contrast, in a world where the only relevant games are simple cake-division problems, the role and structure of justice would be quite different. A specific aspect of that is also stressed by Hayek. In “many instances”, writes Hayek, distributive outcomes would have to be regarded as “very unjust” if they were the result of “deliberate allocation to particular people” (1976, 64).

Hayek has rendered us a great service by insisting on a conceptualization of justice as a property of institutionalized structures of interaction instead of plain distributive justice. Indeed, he seems to have been one of the few (apart from Bedau (1978) and a limited strand of discussions following that) who stressed this important Humean aspect of Rawls’s work. Moreover, his challenge serves as a constant reminder that we should keep in mind the significance of (A)–(D) for getting “social justice” off the ground, theoretically and politically. More specifically, dynamic capitalism may be subject to transformative changes possibly affecting this relevant set of assumptions. It cannot be ruled out that this may bring about a situation where social justice (in the sense defended here) is indeed a mirage. If this situation were caused by (D), while (A)–(C) continue to hold, Schmolter would probably not be the only one to diagnose a deep crisis of our civilization.

## 5. The Dichotomy of Markets and Politics

The conception discussed in this section is close to some models of textbook economics. At the same time, it has an affinity with the constructivist rationalist views criticized by Hayek. Stressing the dichotomy between *distribution/justice* and *allocation/efficiency*, it sets the scene for a strict separation of economic and political spheres. This separation was suggested by Walras<sup>16</sup> and is cris-

<sup>16</sup> Walras (1977, lesson 2) suggests a foundational distinction between (i) *science pure naturelle* (regarded as science proper) concerned with the relations between things,

ply expressed in Abba Lerner's AEA-presidential address. According to Lerner, the domain of economics is defined by solved political problems: "... the solution is essentially the transformation of the *conflict* from a political *problem* to an economic *transaction*. An economic transaction is a solved political problem. Economics has gained the title of queen of the social sciences by choosing *solved* political problems as its domain" (1972, 259, emphasis in original).

In analytical terms, this distinction of spheres is expressed by the Two Theorems of Walrasian General Equilibrium Economics. As shown by the Two Theorems, overall problems of economic welfare may be decomposed into two separate steps: as a first step, determining the pattern of initial endowments is a problem of "classical" distributive justice (not social justice à la Rawls), which is "solved" by politics, or politics assisted by social philosophers supposedly knowing what the just distribution is. The second problem is solved by the market mechanism. According to the Second Theorem, the market is apt in bringing about any Pareto efficient allocation which is recommended by whatever distributive criterion, provided that the pattern of initial endowments is in the first step appropriately adjusted by lump-sum taxes and transfers.

In a nutshell, Lerner summarizes a fascinating vision of the market as a sphere of pure allocation, separated from the mediation of conflictual distributive issues by political compromise, ethical norms, or power. From this starting point, the persuasive logic of depoliticized, trade-mediated division of labour can be made explicit. We may view the market (as Samuelson put it) as a method of coercion, but it is a kind of coercion which (properly understood) ought to be uncontested: all of us (as producers) are coerced to the benefit of all of us (as consumers). No additional criterion of justice or accountability needs to be invoked, as the market mechanisms constantly hold all of us accountable for the opportunity costs caused by our actions. In Rawls's classificatory scheme (see footnote 6), the market of the Two Theorems approaches perfect procedural justice.

I cannot pick up on all the merits of this model here. It helps to organize our thinking in various respects and proves valuable as a point of critical departure

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(ii) applied science (*l'art*) with the relation between humans and things as subject matter and (iii) the moral sciences concerned with the relations between humans. These three branches have (i) truth, (ii) utility and (iii) justice as their respective branch-specific core criteria. In economics, the division of labour between the three branches can be described as follows:

- "pure economics" is concerned with the logic of exchange and exchange value as a natural and mathematical fact,
- "applied economics" deals with the conditions of production, and
- "social economics" as a moral science is concerned with distribution. Walras thinks that pure economics is in a position to disambiguate issues relevant for social economics which otherwise would remain a puzzle, but that its world of mathematical truth is not contaminated by influences from the messy world of social economics.

for considering various kinds of constraints and imperfections. Most notably, it allows for assessing the excess burden of interferences with the invisible hand of the market: re-distributive taxation which is affecting (“distorting”) the price system. To be sure, such insights have to be taken on board by anybody who wishes to implement schemes of social justice.

However, the Walras-Lerner world is related to two problematic tendencies in mainstream economics: the tendency to consider (re-)distribution as a technocratic exercise and the tendency to consider distribution as something outside the proper concern of economics. (The criticism of mainstream economics is often that it is the professional task of economists to focus on the wealth-enhancing potentials of the market, not the distribution of wealth.) The latter tendency is often coupled with a skeptical view regarding redistribution and/or some degree of dismissiveness regarding distribution as an aspect of research strategies in (pure) economics, which occasionally culminates in verdicts like the following: “Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion the most poisonous, is to focus on questions of distribution” (Lucas 2004, 13).

Neither of these tendencies are good or bad per se. They are, however, problematic to the extent that in real-world environments conditions (A)–(D) obtain. Notice that Lerner’s formula does not interfere with the “Rawlsian” conditions of social justice (A) and (D), but with (B) and (C). B implies some transactions generating a surplus which is not automatically distributed by a competitive factor prices/remunerations; C implies systematic effects of social structure.

In the past 25 years, there has been an increasing amount of work by economists supporting the plausibility of (B) and (C). With considerable relevance for (C), empirical work succeeded in “bringing distribution in from the cold,” as demanded by Tony Atkinson (1997). This includes work on the interdependence of norms, social structure and social mobility, which is directly relevant for condition (C). To give an example which recently has been the subject of some debate: “inequality” according to some measure of income distribution may be found to be associated with a low degree of social mobility, as suggested in the empirical findings summarized as “The Great Gatsby Curve” (see Corak 2013). Irrespective of the specific slope of such “curves,” findings of this kind call for studying the mechanism(s) mediating pertinent interdependencies and the conditions triggering these mechanisms.

Condition (B) is directly supported by the models of contested exchange and incomplete contracts, which can be shown to be relevant for labour markets and other more complex markets (see for instance Bowles 2004). Such developments beyond the traditional models of pure exchange are supported by behavioural and evolutionary game theory. Progress has been made with regard to the problematic assumptions supporting the Two Theorems, including not

only the non-availability of lump-sum taxes and transfers, but also analyses questioning the separability of allocation and distribution in worlds with public goods.

Some recent work by economists is also relevant in a broader sense of the complementarity between political philosophy and social theory stressed by Miller (1999, 43). It contributes to interdisciplinary research on justice. First, game theorists, behavioral economists<sup>17</sup> and social psychologists<sup>18</sup> deal with the socio-economic explanations of justice-related norms and the relevance of reciprocity, fairness, and the endogeneity of preferences and behavioral traits. Ken Binmore's *Natural Justice* (2005) provides the architecture of what can be considered as a Humean approach supplemented by game theory. Second, researchers concerned with distributive issues and normative economics use the notion of social justice (see Atkinson 1983) or "the just economy" (see Meade 1976) when they wish to combine the different dimensions of distributive justice with issues reaching beyond what is normally considered as distributive justice, including social mobility and intergenerational transmission. Empirical researchers with a strong theoretical background such as Atkinson are particularly aware of this multi-dimensionality and concomitant interdependences.

However, the Walras-Lerner view is still contributing to shaping pre-analytic visions, organizing the thought about justice in a direction which is at odds with an understanding of "justice as the first virtue of institutions" in Rawls's sense. It may influence the attitudes towards distributive justice among economists: seen from a Rawlsian (or Schmollerian) perspective, some of them are overly technocratic, whereas others are unduly agnostic or even nihilistic.

As was argued above, there are good reasons to stress the significance of social justice à la Rawls et al. However, the Walras-Lerner framework suggests a specifically well-defined normative-institutional division of labour (related to the dichotomy distribution/justice vs. allocation/efficiency). This should be considered as a permanently useful challenge. Whether it is a good theoretical basis for institutional design and policy depends on whether the problems underlying conditions B and C diminish in importance.

## **6. Concluding Remarks: Cheers for Hayek, the Social Justice Theorist**

Social justice can be defended as a meaningful concept, even though the defence hinges upon necessary conditions which may be empirically falsified. In

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<sup>17</sup> For introductory expositions of this line of research, see e.g. Bowles (1998; 2004) and Peter Corning (2011).

<sup>18</sup> See, for instance, Mikula (2002).

this paper I discussed theories inimical to the idea of social justice at some length, as they may be helpful for further developing the concept of social justice. First, they show us conceptual alternatives. Second, they provoke a more thorough discussion of the crucial conditions for social justice at a conceptual, empirical and practical level. Determining the status of social justice requires analysis of the factual “circumstances of justice,” which may change throughout the evolution of capitalist market economies. For instance, social justice may have been meaningful and historically relevant for the development of institutional frameworks in progressing national economies throughout much of the 19<sup>th</sup> and 20<sup>th</sup> centuries, but its role in the globalized world of the 21<sup>st</sup> century may appear in a different light.

One aspect of Hayek’s (1976) reasoning concerns a question related to his moderate pessimism regarding the political sector: does the role, the scope and the nature of factually employed normative standards (e.g. “social justice”) tend to be *congruent* with what is implied by our knowledge of how social institutions function? While Schmolter’s idealist psychology seems to induce some optimism on the question, Hayek clearly thinks differently. Correcting the presently diagnosed incongruence is *the* main challenge for him. Be that as it may, Hayek is right in pointing out that factually employed standards may be misguided or somehow problematic. Their (perhaps even genetically hard-wired) behavioural roots may have been developed in games of a type which are no longer centre stage in the prevailing institutional setting. Moreover, the vicissitudes of the public discussion may play a further role in distorting normative standards in one direction or the other: there is no obvious mechanism making sure that political ideas about the scope and direction of deliberate institutional change – and concomitant ideas about political accountability and social justice – are always congruent with the nature of problems (which may change quite rapidly). Hayek’s (1976) critique of the “mirage of social justice” is supplemented by some conjectures pointing in that direction.

The scope of deliberate politically mediated change may indeed sometimes be overstretched, sometimes played down. Deliberate change may indeed be informed by false principles. Given the complexity of interdependences and feedback effects, such a kind of distortion may last for a while – perhaps for an era of several decades. Even when the drawbacks of the incongruence do materialize in the form of negative feedbacks, they are not immediately understood in their causal relation to the pertinent incongruence. This may lead to a malfunctioning of the political sector such that condition D no longer obtains.

Hayek’s conjectures can be taken as an encouragement for pertinent empirical research. Suppose now that this research confirms Hayek’s (moderate) pessimism for a given historical/geographical context. Should this induce us to abandon “social justice?” No. While the prospects of social justice in a globalizing world are indeed contingent upon conditions which certainly cannot be

taken for granted, the conceptions of social justice discussed in this paper are indispensable. They are indispensable not despite, but because the concerns just sketched need to be taken seriously. None of the protagonists of social justice discussed in the present paper, including Schmolter, endorsed the kind of technocratic approach rejected by Hayek as “constructivist” overstretching of the scope of deliberate change. All of them (in one way or the other) stressed the complexity of modern society and its multiple spheres of social interaction. In particular, Rawls’s “social justice as the first virtue of institution” is developed for providing guidance in the context of non-technocratic improvement in pluralistic societies, taking into account various kinds of imperfections and constraints. Much of this is close to Book VI of Adam Smith’s *Theory of Moral Sentiments* (1790, ii.2.7 ff.), whose anti-technocratic passages on the “man of system” (*ibid.*, ii.2.17) are of emblematic significance in a Hayekian context.

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