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Ethical Maturity and Economic Progress: Adam Smith's Lesson Still Applies*

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As Vernon Smith argued, "markets economize on the need for virtue, but do not eliminate it." The need for a virtuous, ethically mature citizenry is an important but often-overlooked theme in Adam Smith. Unethical business behavior creates a demand for government regulation ostensibly to fix the problem; however, evidence that government regulation reduces economic growth suggests that this does not so much solve the old problem as it creates new ones. Using what we know about "rational irrationality" and people's views on government, we explain why unethical business behavior leads to a higher demand for government intervention and why that intervention is not likely to create a more ethically mature society.

From Moral Sentiments to the Wealth of Nations

Adam Smith, the father of modern economics, was a moral philosopher before he was an economist: The first edition of his first book, *The Theory of Moral Sentiments* (*TMS*), predates the first edition of *An Inquiry into the Nature and Causes of the Wealth of Nations* (*WN*) by almost two decades—1759 versus 1776—and the sixth and final edition of *TMS* was published in 1790, the same year Smith died. Scholars highlighted what they thought was a tension between the Smith of *TMS* and the Smith of *WN*: Imaginatively called *Das Adam Smith Problem*, the supposed tension between the other-regardingness of *TMS* and the self-interestedness of *WN* has been a running theme in Smith scholarship.[1]

The two are not in tension, however. As Jerry Evensky argues, ethical maturity among a citizenry, according to Smith, was at the foundation of his "obvious and

simple system of natural liberty" and, therefore, at the foundation of a prosperous and flourishing society.[2]

Persons are complex creatures. In Smith's framework, they cannot be reduced to the pure other-regarding benevolence of some of our loftier moral and religious visions or the pure self-regarding prudence of the narrowest economic models. People, for Smith, have unavoidable moral and intellectual limitations. This made him an exemplar of what Thomas Sowell called "the constrained vision."[3] Smith's project sought to identify the ways in which institutions channeled our moral incompleteness and imperfection for good or ill, socially speaking.[4] His moral project helped us navigate the often choppy waters between anarchy and leviathan, and he sought to highlight and understand the "moral sentiments" that made for social harmony in a world where trade connected people more and more closely.[5]

Smith's overall project is an integrated whole that encompasses *TMS*, *WN*, and his unpublished *Lectures on Jurisprudence*. It is easy to misinterpret Smith's claims about "self-love" without understanding its broader context and especially the notion of "sympathy" that he develops in *TMS*.[6] "What else is required," Smith asked, but "peace, easy taxes, and a tolerable administration of justice" to raise a society from barbarism to prosperity? While Smith emphasizes the importance of secure private property rights, there is more to prosperity specifically and flourishing generally than merely security. Ethical maturity matters, as well, because of free-rider problems in what David Rose calls the "cultural commons."[7] Bad business behavior—which can happen more frequently than might be socially optimal due to monitoring problems in corporations, large organizations, and large societies—creates demand for regulation on the part of voters afflicted with what Bryan Caplan calls "anti-market bias."[8] To borrow a framing made famous by Bruce Yandle, executive malfeasance creates new "Baptists" who want additional regulation on moral grounds.[9]

Ethical maturity, therefore, is necessary if the "obvious and simple system of natural liberty" is to endure and for a society to enjoy "peace, easy taxes, and a tolerable administration of justice." This is at odds with the caricature of what people think of as free-market capitalism: "In the popular mind—and not only in the popular mind—capitalism is more often than not associated with unleashed greed and the pursuit of pleasure."[10] The (im)moral actions of businesspeople inform the citizenry's understanding of the political legitimacy of a commercial society and give people the (mistaken) view that commerce is self-absorbed rather than self-loving in the way Smith discusses it.[11]

To interpret Smith's system as an apologetic for untrammeled, unrestrained, hedonistic greed on the model of (for example) Michael Douglas's character

Gordon Gekko in *Wall Street* is to miss Smith's point. In what follows, we dive deeper into Evensky's interpretation of Smith and explore how ethical maturity leads to economic progress—and how ethical immaturity leads to economic regress. To put it another way, "Smith's moral and political philosophy might serve as a corrective to contemporary neo-liberal theory which conceives of liberty as nothing more than the capricious indulgence of one's passions and holds that any effort by the government to restrain such behavior will inevitably lead to tyranny."[12] Or, as another Smith—2002 Nobel Laureate Vernon Smith—put it, "markets economize on the need for virtue, but do not eliminate it."[13]

Security, Prosperity, and Morality

In *TMS*, Smith points out that security is necessary for a successful liberal society.[14] Smith emphasized the need for a system of justice that establishes and enforces principles of behavior, writing, "That the security which the laws in Great Britain give to every man that he shall enjoy the fruits of his own labour, is alone sufficient to make any country flourish, notwithstanding these [mercantile impediments] and twenty other absurd regulations of commerce."[15] Kalvyas and Katznelson put it this way, "markets constitute the 'system of natural liberty' because they shatter traditional hierarchies, exclusions, and privileges."[16] To Smith, it was not possible to examine questions of morality and individual rights with respect to exchange without a firm theoretical underpinning of consent: "Smith shows how recognizing the right to choose and consent is essential for development to really be beneficial for all. The gains from trade can only occur if one party does not coerce the other, an idea that led Smith to fiercely criticize European conquest and colonization of non-Europeans."[17]

Empirical study of economic freedom suggests that the institutions of limited government, particularly clearly defined and strongly enforced private property rights, promote economic growth.[18] Security of person, property, and promises protects *consent*, an element of the Smithian project that, according to William Easterly, has been underemphasized.[19] Secure private property rights and the institutions of consent-protecting economic freedom promote economic growth: without them, people have weak incentives to exchange and invest.[20] Smith makes it clear that security of persons, property, and promises is necessary for growth. Otteson explains, "Smith considers an observance of the rules of justice to be the minimum level of conduct necessary for a society to survive, because without it no one has security in his person or possessions; and a community, which requires people to work with and among one another, cannot arise or endure in such a state."[21]

Ultimately, however, a cohesive and prosperous social order depends not on government but on an ethically mature, self-governing citizenry.[22] As Smith writes, "What institution of government could tend so much to promote the happiness of mankind as the general prevalence of wisdom and virtue?"[23] In his emphasis on the importance of moral culture and protection of what he calls the "cultural commons," David Rose puts it this way: "High-trust societies are the key to unlocking the unfathomable power of cooperation."[24] An ethically mature citizenry successfully navigates between the Scylla of the Hobbesian war of all against all and the Charybdis of the despotic police state. Attention to virtue becomes more important as the division of labor deepens, as the economy grows more complex, and as monitoring costs increase.

Attaining (and maintaining) such institutions in the first place is a much more difficult problem and does not come from the surgical implantation of institutions by elites or outside observers. An extensive literature exists on the effects of institutions on economic growth, a notable example of which suggests that countries with British legal heritage (common law) tend to perform better than countries with French legal heritage (civil law).[25] Formal institutions matter, but a more complete explanation of this phenomenon must include analysis of informal constraints, such as interpersonal sanctions, taboos, customs, traditions, and codes of conduct.[26]

To Smith, in a liberal society, individuals were free to engage in what he described as the human "propensity to truck, barter, and exchange one thing for another"[27] so long as they do not injure others. Unfortunately, that some people will use liberty badly becomes a pretext for others to seize power: The result might be order without liberty and order without humanity.[28] Smith makes it clear that security of persons and property is necessary for growth, but ultimately a cohesive social order depends not on the government but on a self-governed, ethically mature citizenry.

Creating "Baptists": Ethical Failure and Demand for Regulation

Smith argued that people are drawn to a search for sympathy with one another. He also argued that we have a "taste" for justice, albeit a taste shaped by commerce, as with the Dutch merchants Smith discussed in his *Lectures on Jurisprudence*.[29] This long passage from *TMS* illustrates:

> When we see one man oppressed or injured by another, the sympathy which we feel with the distress of the sufferer seems to serve only to animate our fellow-feeling with his resentment against the offender. We are rejoiced to see

> him attack his adversary in his turn, and are eager and ready to assist him whenever he exerts himself for defence, or even for vengeance within a certain degree. If the injured should perish in the quarrel, we not only sympathize with the real resentment of his friends and relations, but with the imaginary resentment which in fancy we lend to the dead, who is no longer capable of feeling that or any other human sentiment. But as we put ourselves in his situation, as we enter, as it were, into his body, and in our imaginations, in some measure, animate anew the deformed and mangled carcass of the slain, when we bring home in this manner his case to our own bosoms, we feel upon this, as upon many other occasions, an emotion which the person principally concerned is incapable of feeling, and which yet we feel by an illusive sympathy with him. The sympathetic tears which we shed for that immense but irretrievable loss, which in our fancy he appears to have sustained, seem to be but a small part of the duty which we owe him. The injury which he has suffered demands, we think, a principal part of our attention. We feel the resentment which we imagine he ought to feel, and which he would feel, if in his cold and lifeless body there remained any consciousness of what passes upon earth. His blood, we think, calls aloud for vengeance. The very ashes of the dead seem to be disturbed at the thought that his injuries are to pass unrevenged. The horrors which are supposed to haunt the bed of the murderer, the ghosts which, superstition imagines, rise from their graves to demand vengeance upon those who brought them to an untimely end, all take their origin from this natural sympathy with the imaginary resentment of the slain. And with regard, at least, to this most dreadful of all crimes, Nature, antecedent to all reflections upon the utility of punishment, has in this manner stamped upon the human heart, in the strongest and most indelible characters, an immediate and instructive approbation of the sacred and necessary law of retaliation.[30]

Smith's description applies as well to how people react to stories about financial malfeasance. A well-functioning market relies on decentralized historical development of rules, norms, and practices, but people are at times quick to seek sovereign protection and regulation in response to public wrongdoing. This is perhaps due to a misguided belief that moral failings *per se* are at the heart of problems with markets. In this way, an externality of sorts emanates from unethical behavior. Alert commercial entrepreneurs can capitalize on others' moral failings by making sure people know that they are above reproach.

However, alert political entrepreneurs can capitalize on others' moral failings (in the base case) by calling for well-intentioned regulation that might be redundant and counterproductive, or worse, by seizing power and resources for themselves by demagoguing "rationally irrational" voters.[31] Citing Baumol, Powell and Rodet note, "When profits can be made through lobbying or other participation

in the political arena, entrepreneurs will be attracted to unproductive or destructive activities. When profits are more readily available by serving consumers through enhancing efficiency or creating new products, entrepreneurship will be more productive."[32] This mechanism thwarts opportunities for commercial entrepreneurship, increases opportunities for political entrepreneurship, and protects inefficient incumbents from competition.[33] Ethics are important *apart from* considerations of security. Thus, while security is a necessary condition for liberty and prosperity to develop and be sustained in society, its existence is not a sufficient condition.[34]

To many observers, the 2007–2009 financial crisis was symptomatic of a system that rewarded injustice and impropriety through taking advantage of low-income households by offering subprime loans in the years leading up to the crisis. It is easy to see vivid, large-scale failures and read tragic stories about shattered dreams and assume that these failed cases are representative of the entire market system rather than pathological incentives created by housing policy.[35] In a polity infected with "anti-market bias," it is then easy to take a next step and demand government regulation. Such ethical failures make more regulation politically feasible, and corporate malfeasance creates an opportunity for political entrepreneurs to indulge "the people's romance."[36] In this scenario, "rational irrationality" rules as people tend to generalize hastily from the example of bad actors; hence, bad business by companies like Enron tarnishes the reputation of all business.[37]

In 1983, the economist Bruce Yandle introduced the expression "bootleggers and Baptists" to describe political "coalitions" that aren't coalitions in the strict sense and that don't seem, at first glance, to make much sense.[38] He drew his inspiration from the economics of prohibition and argued that alcohol prohibition draws support from "bootleggers" who like seeing their competition eliminated and "Baptists" who supported prohibition for moral reasons. In Yandle's story, the Baptists are crucial because they monitor the regulators and ensure that the rules are enforced. Ethical failures create new "Baptists" who wish to see, for example, more extensive regulation in the banking sector. They unwittingly aid the "bootleggers"—big banks, in this case—and impoverish the citizenry by limiting market entry and making markets less competitive.

Propriety, Ethical Maturity, and Prosperity

Smith's mental device—the impartial spectator—helps us develop intuition about propriety. Easterly explains, "Although formal institutions could enforce these rights to choose, Smith recognized that strong moral principles were even more

powerful to make them happen—and that the right institutions would not emerge without the right moral norms. The right morals for Smith can be summarized with the idea of reciprocity—any rights that I want for myself, I should respect in others."[39]

That is, a flourishing, liberal social order grows in particular ethical soil, and indeed, an ethical soil informed by the ethics of Jesus's Golden Rule. Evensky emphasizes the importance of balance: "In Smith's analysis, proper balance is the key to moral sentiments, and the standard of proper balance is the sympathy of an impartial spectator. The ideal moral sentiments are therefore those that, in measure and balance, enjoy the complete sympathy of a perfectly informed and perfectly ethical impartial spectator. This idealized, abstract spectator knows both the contents of your heart and the ideal moral measure and balance of sentiments."[40]

While enlightened self-interest in this way has significantly positive economic and social consequences, unconstrained pursuit of self-interest narrowly construed can make societies unravel. As Evensky writes, "[I]n Smith's analysis, while self-love is a necessary condition for the unleashing of humankind's productive energy and creativity, it is not sufficient … an unfettered self-interest could undermine a constructive liberal society."[41] Similarly, in his discussion of David Hume, Lionel Robbins wrote that without some idea of justice, "the classical theory of self-interest and the market would remain completely in the air."[42] In the absence of an ethically mature citizenry, we find ourselves in a tension between two extremes: a chaotic war of all-against-all on one hand, and ordered despotism on the other. The more these conditions prevail, the more difficult it is to realize the mutual gains from trade that come from social cooperation under the division of labor. We begin, as Smith notes in book 1, chapter 2 of *WN*, with a recognition that others have rights and interests, and as he further notes in his *Lectures on Jurisprudence*, the pursuit of our own interests in the commercial sector builds up the virtues of "probity and punctuality" much like exercise builds muscle.[43]

Ideally, the impartial spectator would sympathize with our actions and sentiments. An ethically mature citizenry, one in which individuals pay heed to the judgements of an impartial spectator, would thus be constrained in the alignment of their behavior to gain the approval of others. As Smith wrote, "The all-wise Author of Nature has, in this manner, taught man to respect the sentiments and judgments of his brethren."[44] This is required if we are going to have mutually beneficial exchange. "There is no passion," Smith writes, "… concerning whose indulgence we ought so carefully to consult our natural sense of propriety, or so diligently to consider what will be the sentiments of the cool and impartial spectator."[45] He writes about how we respond to social signals: "Man naturally

desires, not only to be loved, but to be lovely; or to be that thing which is the natural and proper object of love. He naturally dreads, not only to be hated; but to be hateful; or to be that thing which is the natural and proper object of hatred. He desires, not only praise, but praiseworthiness; or to be that thing which, though it should be praised by nobody, is, however, the natural and proper object of praise."[46]

As societies grow, monitoring costs rise and the impartial spectator becomes more important. Imperfect second- and third-party monitoring and enforcement requires first-party monitoring and enforcement. While markets are able to function well enough without needing individuals to deeply care about one another in the manner of a family member, this functionality is likely to break down if market behaviors such as lying, cheating, or stealing are not condemned by informal norms and formal institutions. In this manner, secure property rights and the rule of law are necessary but not sufficient for prosperity.

Reputations go a long way toward solving collective action problems out of simple prudence. As Vernon Smith writes, "Once a continuing trading relationship is established across time, the reciprocal benefits of exchange provide the foundation for self-enforcing property rights."[47] Repeated interaction constrains cheating because a reputation for honesty will mean more opportunities to trade while a reputation for dishonesty will mean fewer opportunities to trade. Contrary to popular belief, commercial society is "more likely to be morally decent," not less.[48]

Market forces do not completely eliminate cheating, however; cooperation sometimes breaks down. When cheating is detected, it can have important spillover effects because it affects voters' and policymakers' beliefs about business. People are attracted to relatively simple stories featuring clearly defined villains they can decry and clearly defined victims with whom they can sympathize. Political entrepreneurs are all too happy to market themselves as purveyors of "justice" in the form of punishment for the villains and relief for the victims.

Importantly, the proposed remedies need not actually fix the problem and will likely have negative unintended consequences. Dawson and Seater, for example, show that regulation leads to lower economic growth.[49] Voters and commentators, however, have weak incentives to take this into account or to think about how markets and reputation mechanisms might solve information problems. They are likely to be hungry for "justice." As Bryan Caplan has argued, people tend to have "rationally irrational" beliefs about economic policy: The beliefs are "irrational" in that they do the opposite of what voters claim to want. For example, voters are enthusiastic about tariffs even though they make people worse off, on net. People still cling to these beliefs because changing them is

almost all cost and no benefit. Just as a voter has an incentive to cling to the good feelings they get from their enthusiasm for border walls and tariffs, they have incentives to cling to government regulation as an alleged solution to problems of bad business ethics even when such regulation will be ineffective or counterproductive. Economic crises produce witch hunts, and businesspeople are attractive targets.

This is one of the reasons why ethical maturity matters so much. Trade associations internalize collective action problems to a degree, but they can (and do) turn into rent-seeking operations easily.[50] People care about others, but we do not literally share others' experiences. We cannot see into their hearts and minds. Hence, Smith writes that we can only conceive of what others feel "by conceiving what we ourselves should feel in the like situation."[51] We are, in short, endowed with a capacity for sympathy, but our capacity for sympathy has limits. We face an almost intractable problem with constructing "the other," largely meaning people who are outside our communities and with whom entering into sympathy is difficult. In attempts to avoid offense, however, we overstep civility by agitating for the passage of new regulations and laws, making it even more difficult for people to exchange.

Like Smith, we are not at all sure that a regulatory "cure" will not be worse than the ethical disease. In his analysis of the Great Depression, Higgs coined the term *regime uncertainty*, referring to the public uncertainty that arose regarding what policies the Roosevelt administration would enact.[52] Claiming that regime uncertainty was a significant driver of the dampened investment spending that prolonged the Great Depression, Higgs cites financial economist Benjamin Anderson, who wrote, "The impact of these multitudinous measures—industrial, agricultural, financial, monetary, and other—upon a bewildered industrial and financial community was extraordinarily heavy."[53] Higgs argues that the Roosevelt administration's misguided diagnosis of the Depression as a problem of unethical, rampant speculation (as opposed to monetary mistakes) and the ensuing policy response actually helped to prolong and deepen the Depression. Roosevelt nonetheless remains a consensus favorite among historians and the general public in no small part for his enthusiastic willingness to supply the "bold, persistent experimentation" the country supposedly demanded.[54]

A similar phenomenon occurred during and after the crisis of 2007–2009, as many firms and banks sat on small mountains of cash because they were hesitant to invest, in no small part due to fear of ongoing financial crisis and policy uncertainty.[55] Echoing discussions of the Great Depression-era recovery, Dwyer and Lothian of the Federal Reserve Bank of Atlanta pointed to regime uncertainty as one of the causes of the slow economic recovery in the years following the

financial crisis.[56] In the meantime, bankers, investors, and the wealthy got an increasingly bad name during the financial crisis and its aftermath, as Wall Street and other locations were "occupied" by protestors who were upset with what they thought was an inequitable distribution of resources and political power.

The potential for regulation to privilege the few at the expense of the many had never been lost on Smith, but he got to see it up close during his time working as a Commissioner of Customs. It informed his 1785 update to *WN*, of which Evensky writes that he "thus [had] seen from the inside how these mercantile interests worked to secure their advantages through legislation…. In that revision [Smith] writes that this partial, mercantile interest has expanded its power through sophistry and persuasion and, when those have failed, by intimidation."[57] It is the kind of behavior that would be roundly rejected by the impartial spectator.

Conclusion

Security is necessary for economic progress, but it is not sufficient. For Adam Smith, the substance of economic progress was not untrammeled greed and indulgence of every appetite in the service of the crudest kinds of self-interest. Ethical maturity among the citizenry was of foremost importance because it is essential to the political legitimacy of market institutions. Ethical immaturity by rogues within the commercial sphere increases demand for centralized government regulation—a demand that is stable and persistent due to voters' incentives and which political entrepreneurs are generally happy to supply.

As Evensky argues, ethical maturity is essential to a successful liberal society.[58] Building on the Smithian project, still others have pointed out how ethical maturity makes a high-trust society (and therefore prosperity) possible. People want not only to be loved but also to be lovely, and we naturally empathize with victims of injustice. One problem is that what is "lovely" with reference to a small in-group may not be particularly "lovely" to a broader society. This means that bad business behavior produces negative spillovers that degrade the cultural commons and, perhaps, induces regulatory responses that are politically rational but economically unwise. If liberty and prosperity are going to endure, an ethically mature citizenry is necessary. Adam Smith said so. We—and many others—think he was right.

Notes

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1. For discussions, see, among many others, Robert A. Black, "What Did Adam Smith Say about Self-Love?" *Journal of Markets and Morality* 9, no. 1 (Spring 2006): 7–34; Jerry Evensky, "Adam Smith's *Theory of Moral Sentiments*: On Morals and Why They Matter to a Liberal Society of Free People and Free Markets," *Journal of Economic Perspectives* 19, no. 3 (2005); idem, *Adam Smith's Moral Philosophy: A Historical and Contemporary Perspective on Markets, Law, Ethics, and Culture* (New York: Cambridge University Press, 2005); James Halteman and Edd Noell, *Reckoning with Markets: Moral Reflection in Economics* (New York: Oxford University Press, 2012); Ryan Hanley, *Adam Smith and the Character of Virtue* (New York: Cambridge University Press, 2009); James R. Otteson, *Adam Smith's Marketplace of Life* (Chicago: University of Chicago Press, 2002); idem, *The Essential Adam Smith* (Vancouver: Fraser Institute, 2018); idem, *Honorable Business: A Framework for Business in a Just and Humane Society* (Oxford: Oxford University Press, 2019); David C. Rose, *The Moral Foundation of Economic Behavior* (Oxford: Oxford University Press, 2011); idem, *Why Culture Matters Most* (Oxford: Oxford University Press, 2019); Eric Schliesser, *Adam Smith: Systematic Philosopher and Public Thinker* (Oxford: Oxford University Press, 2017); Vernon L. Smith, "The Two Faces of Adam Smith," *Southern Economic Journal* 65, no. 1 (1998): 1–19; E. G. West, *Adam Smith* (New Rochelle, NY: Arlington House, 1969); Barry R. Weingast, "The Many, Diverse 'Main Points' of Adam Smith's the *Wealth of Nations*," unpublished paper, 2018.

2. Evensky, "Adam Smith's Theory"; idem, *Adam Smith's Moral Philosophy*.

3. Thomas Sowell, *A Conflict of Visions: Ideological Origins of Political Struggles* (New York: Basic Books, 2007).

4. Jerry Z. Muller, *Adam Smith in His Time and Ours: Designing the Decent Society* (Princeton: Princeton University Press, 1993), 82.

5. J. M. Buchanan, *The Limits of Liberty: Between Anarchy and Leviathan*, The Collected Works of James M. Buchanan, vol. 7 (Indianapolis: Liberty Fund, 1975); Muller, *Adam Smith*, 95.

6. Black, "What Did Adam Smith Say?" 7.

7. Rose, *Why Culture*, 32.
8. See Bryan Douglas Caplan, *The Myth of the Rational Voter: Why Democracies Choose Bad Policies* (Princeton: Princeton University Press, 2007), 31.
9. Bruce Yandle, "Bootleggers and Baptists: The Education of a Regulatory Economist," *Regulation* 7, no. 3 (1983): 12–16. See also Bruce Yandle and Adam Smith, *Bootleggers and Baptists: How Economic Forces and Moral Persuasion Interact to Shape Regulatory Politics* (Washington, DC: Cato Institute, 2014).
10. Muller, *Adam Smith*, 194.
11. See, for example, Black, "What Did Adam Smith Say?"
12. Muller, *Adam Smith*, 188.
13. Vernon L. Smith, "Constructivist and Ecological Rationality in Economics," Nobel Prize Lecture, Stockholm, Sweden, December 8, 2002.
14. This discussion relies on and draws from Evensky, "Adam Smith's Theory"; idem, *Adam Smith's Moral Philosophy*.
15. Adam Smith, *The Theory of Moral Sentiments* (1790; repr., Indianapolis: Liberty Fund, 1982), 540.
16. A. Kalvyas and I. Katznelson, "The Rhetoric of the Market: Adam Smith on Recognition, Speech, and Exchange," *Review of Politics* 63, no. 3 (2001): 550.
17. William Easterly, "Progress by Consent: Adam Smith as Development Economist," *Review of Austrian Economics* (2019): 2.
18. For a review of the literature, see Joshua Hall and Robert Lawson, "Economic Freedom of the World: An Accounting of the Literature," *Contemporary Economic Policy* 32 (2014): 1–19.
19. Easterly, "Progress by Consent." The "persons, property, and promises" framing is from Otteson, *Essential Adam Smith*, 21.
20. For a review of the empirical literature on economic freedom and growth, see Hall and Lawson, "Economic Freedom."
21. Otteson, *Adam Smith's Marketplace*, 139.
22. Evensky "Adam Smith's Theory"; Rose, *Moral Foundation*; idem, *Why Culture*.
23. Adam Smith, *Theory of Moral Sentiments*, 540.
24. Rose, *Why Culture*, 32, viii.

25. On the "Legal Origins Thesis," see, for example, R. La Porta et al., "Legal Determinants of External Finance," *Journal of Finance* 52 (1997): 1131–50; idem, "Law and Finance," *Journal of Political Economy* 106, no. 6 (1998): 1113–55. For competing theories of institutions and development, see Daron Acemoglu et al., "The Colonial Origins of Comparative Development: An Empirical Investigation," *American Economic Review* 91, no. 5 (2001): 1369–1401; R. La Porta, F. López-de-Silanes, and A. Shleifer, "Economic Consequences of Legal Origins," *Journal of Economic Literature* 46 (2008): 285–332; J. Du, "Institutional Quality and Economic Crises: Legal Origin Theory versus Colonial Strategy Theory," *Review of Economics and Statistics* 92, no. 1 (2010): 173–79; Friedrich Hayek, *Law, Legislation, and Liberty*, vol. 1: Rules and Order (London: Routledge, 1973).

26. See the emphasis on ethics in Douglass C. North, *Institutions, Institutional Change, and Economic Performance* (Cambridge, UK: Cambridge University Press, 1990); Deirdre Nansen McCloskey, *The Bourgeois Virtues: Ethics for an Age of Commerce* (Chicago: University of Chicago Press, 2006); idem, *Bourgeois Dignity: Why Economics Can't Explain The Modern World* (Chicago: University of Chicago Press, 2010); idem, *Bourgeois Equality: How Ideas, Not Capital or Institutions, Enriched the Modern World* (Chicago: University of Chicago Press, 2016).

27. Smith, *Theory of Moral Sentiments*, 25.

28. On this we paraphrase Sheldon L. Richman, "Fascism," in *The Concise Encyclopedia of Economics* (Indianapolis: Liberty Fund, 2008), 172–74.

29. Adam Smith, *Lectures on Jurisprudence* (1978; repr., Indianapolis: Liberty Fund: 1982), 538–39.

30. Smith, *Theory of Moral Sentiments*, 70–71, 2.1.2.5.

31. On the relationship between economic freedom and productive versus unproductive entrepreneurship, see Russell Sobel, "Testing Baumol: Institutional Quality and the Productivity of Entrepreneurship," *Journal of Business Venturing* 23 (2008): 641–65. On the problem of rational irrationality, see Caplan, *Myth*.

32. B. Powell and C. Rodet, "Praise and Profits: Cultural and Institutional Determinants of Entrepreneurship," *Journal of Private Enterprise* 27, no. 2 (2012): 19–42; William Baumol, "Entrepreneurship: Productive, Unproductive, and Destructive," *Journal of Political Economy* 98, no. 5 (1990): 892–921.

33. For an example of this mechanism at work in the example of the effects of new banking regulation on small banks after the Financial Crisis, see Hester Peirce, Ian Robinson, and Thomas Stratmann, "How Are Small Banks Faring under Dodd-Frank?" Mercatus Center Working Paper, February 2014, https://www.mercatus.org/system/files/Peirce_SmallBankSurvey_v1.pdf. In a survey of over 200 small banks (defined

as having less than $10 billion in assets), a large majority viewed Dodd-Frank as, "more burdensome than the Bank Secrecy Act, a regulatory regime that banks widely regard as very burdensome. The participating banks noted their substantially increased compliance costs in the wake of Dodd-Frank, [including] new compliance-personnel hires, increased reliance on outside compliance experts, additional resources allocated to compliance, and more time spent by noncompliance employees on compliance."

34. See, for example, McCloskey, *Bourgeois Dignity*.

35. Thomas Sowell, *The Housing Boom and Bust*, rev. ed. (New York: Basic Books, 2010); Robert E. Wright, *Financial Exclusion: How Competition Can Fix a Broken System* (Great Barrington, MA: American Institute for Economic Research, 2019), 117.

36. Daniel B. Klein, "The People's Romance: Why People Love Government (As Much as They Do)," *Independent Review* 10, no. 1 (2005): 5–37.

37. Caplan, *Myth*.

38. Yandle, "Bootleggers and Baptists." See also Yandle and Smith, *Bootleggers and Baptists*.

39. Easterly, "Progress by Consent," 13.

40. Evensky, *Adam Smith's Moral Philosophy*, 117.

41. Evensky, "Adam Smith's Theory," 110–11.

42. Lionel Robbins, *The Theory of Economic Policy in English Classical Political Economy* (London: MacMillan, 1953), as quoted in Easterly, "Progress by Consent," 16.

43. Smith, *Lectures*, 538–39.

44. Smith, *Theory of Moral Sentiments*, 128.

45. Smith, *Theory of Moral Sentiments*, 38.

46. Smith, *Theory of Moral Sentiments*, 113–14.

47. Smith, *Two Faces*, 6

48. Muller, *Adam Smith*, 205

49. John Dawson and John Seater, "Federal Regulation and Aggregate Economic Growth," *Journal of Economic Growth* 18, no. 2 (2013): 137–77.

50. See, for example, Dennis Coates, Jac C. Heckelman, and Bonnie Wilson, "Special-Interest Groups and Growth," *Public Choice* 147, no. 3/4 (2011): 439–57.

51. Smith, *Theory of Moral Sentiments*, 9.

52. Robert Higgs, *Crisis and Leviathan* (Oxford: Oxford University Press, 1987).

53. Benjamin M. Anderson, *Economics and the Public Welfare: A Financial and Economic History of the United States, 1914–46* (1949; repr., Indianapolis: Liberty Press, 1979). For a full treatment of regime uncertainty, see Robert Higgs, *Crisis and Leviathan* (Oxford: Oxford University Press, 1987); idem, "Regime Uncertainty: Why the Great Depression Lasted So Long and Why Prosperity Resumed after the War," *Independent Review* 1, no. 4 (1997).

54. Franklin Delano Roosevelt, Address at Oglethorpe University, May 22, 1932, https://www.presidency.ucsb.edu/documents/address-oglethorpe-university-atlanta-georgia.

55. On the role of Federal Reserve Bank policy and the policy push for "affordable housing" that contributed to the boom and bust, see Sowell, *Housing Boom*; Wright, *Financial Exclusion*, 117.

56. On regime uncertainty in the recovery from the 2007–2009 financial crisis, see Gary Becker et al., "Uncertainty and the Slow Recovery," *Wall Street Journal,* January 2010, https://www.wsj.com/articles/SB10001424052748703278604574624711732528426; idem, "The Slow Economic Recovery-Becker," *The Becker-Posner Blog*, June 2011, www.becker-posner-blog.com/2011/06/the-slow-economic-recovery-becker.html.

57. Evensky, *Adam Smith's Moral Philosophy*, 197.

58. Evensky, "Adam Smith's Moral Theory"; idem, *Adam Smith's Moral Philosophy*; Rose, *Moral Foundations*; idem, *Why Culture*.