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# A European Social Model of State-Market Relations\*

## The Ethics of Competition from a “Neo-liberal” Perspective

MICHAEL WOHLGEMUTH\*\*

### *Ein Europäisches Sozialmodell der Beziehungen zwischen Staat und Markt – Die Ethik des Wettbewerbs aus ‚neo-liberaler‘ Sicht*

*In this paper I portray „neo-liberalism“ in its original conceptual meaning as opposed to the generic term of depreciation as which it is commonly used. I identify fair competition and the denial of all privilege as the major concerns of original neo-liberals. Ethical merit for competition might, at first sight, be based on only two principles: individual natural rights (equal liberty) and socially desirable outcomes (“unintended altruism”). It was the neo-liberal idea to put fairness-norms or universally applicable rules of just behaviour between an unqualified “input-based” ethics and an unqualified “output-based” ethical consequentialism. The enforcement of such rules is a major obligation of the state. Today, the European Union assumes the role of “guardian” of competition. In a certain, but limited sense, neo-liberalism, correctly understood, can be argued to be the one founding “European Social Model”. However, beyond the realm of core of common, universalisable interests, competition amongst social-political models seems a preferable option for Europe.*

*Keywords: Neo-liberalism, Ordo-liberalism, European Social Models, Ethics of Competition*

#### 1. Introduction: the spectre of neo-liberalism

The Communist Manifesto, published in 1848, opens with these dramatic lines:

“A spectre is haunting Europe – the spectre of Communism. All the Powers of old Europe have entered into a holy alliance to exorcise this spectre: Pope and Czar, Metternich and Guizot, French Radicals and German police-spies. Where is the party in opposition that has not been decried as Communistic by its opponents in power? Where the Opposition that has not hurled back the branding reproach of Communism, against the more advanced opposition parties, as well as against its reactionary adversaries? Two things result from this fact: I. Communism is already acknowledged by all European Powers to be itself a Power. II. It is high time that Communists should openly, in the face of the whole world, publish their views, their aims, their tendencies, and meet this nursery tale of the Spectre of Communism with a Manifesto of the party itself.” (Engels/Marx 1848/2005: 1)

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150 years later, the spectre of Communism has been mostly dispelled. In its place a new spectre is today haunting “old Europe”: Neo-liberalism. If one replaces the word “Communism” with “Neo-liberalism”, Marx’s quote offers a rather accurate description of today’s political and intellectual climate. Today, neo-liberalism serves as a “branding reproach” that helps enormously in discrediting political adversaries of all sides. The effect of this branding is that no one today wants to be “neo-liberal” and that there is in fact no 21<sup>st</sup> century neo-liberal “Manifesto of the party itself”.

In this paper, I offer no such Manifesto either, but rather an account of well established historical ordo- or neo-liberal views concerning state-market relations with special emphasis on the role of competition and the ethical value that has been, and still can be, attached to it. I start with a short account of the history of ideas of original neo-liberalism and the perhaps surprisingly active role self-declared neo-liberals attached to the state (parts 2 and 3). Part 4 presents several ethical vindications of open, competitive markets stressed by neo-liberals: equal liberty, procedural justice, reduction of private (and state) power and the unintended, but effective, “altruism” of consequences. Part 5 describes a few central legal-institutional implications of this view and part 6 offers a rough assessment of neo-liberal elements to be found on a European Union level. Part 7 concludes with a plea for an equally open and rules-based competition amongst social models in Europe.

## **2. A short history of neo-liberalism**

Many commentators see neo-liberalism as a right-wing Anglo-Saxon capitalist conspiracy that somehow invented globalisation, privatisation and unfettered markets, thus implying that neo-liberalism was an ideology of the 1980s, fostered by a few powerful politicians such as Margret Thatcher or Ronald Reagan who were instructed by a few spin-professors such as Milton Friedman or Friedrich von Hayek (see e.g. Klein 2007 or Chomsky 1999). The actual history of neo-liberalism is, however, dramatically different.

Neo-liberalism was invented in Paris, France, Europe. And the year was 1938. At that time, the spectre of totalitarianism was, in fact, haunting our continent. Liberalism was dead; fascism and communism were the dominant beliefs in politics and, even more so, amongst intellectuals and clerks in Europe at that time. Both a sense of failed and misconceived “old”, “classical” or “laissez-faire” liberalism and the imminent threat that totalitarianism posed to European civilisation led to a first (and for many years, last) meeting of some 25 intellectuals who still believed in the virtue of individual liberty. These intellectuals took it upon themselves to re-assess liberalism as a political programme for a most troubling future. Historians of ideas know the event as the “Colloque Lippmann”. Jacques Rueff invited scholars from Europe (German and Austrian participants had to come from exile) to discuss the need for a “*rénovation du libéralisme*”, beginning with challenging ideas just published by Walter Lippmann in his book on *The Good Society* (Lippmann 1938). Among those attending who are still known today were: Raymond Aron, Friedrich von Hayek, Ludwig von Mises, Michael Polanyi, Wilhelm Röpke, Louis Rougier, and Alexander Rüstow.

Walter Lippmann, in his opening address, defined the purpose of the meeting to be the need to find a common intellectual basis for anti-totalitarianism. In his view, it

would be useless to try to “reaffirm and resurrect the formulas of 19<sup>th</sup> century liberalism”, since the old doctrine and/or its political realisation had laid the causes for its own decline. The old doctrine had allowed “monopoly capitalism” to discredit the market economy and to thus distort a “synthesis of order and liberty”. Hence, according to Lippmann, liberalism would have to be rebuilt, not merely renovated (Colloque Lippmann 1938: 20 and 27)<sup>1</sup>. During the ensuing discussion, only Mises defended “liberalism” without any qualifications – or, as he put it, concessions to the totalitarian fashions of the time (ibid.: 31). Most other discussants seemed more than ready to be rid of any allegiance to “old”, “laissez-faire” or “Manchester”-liberalism, and rallied around the flag of “néo-libéralisme” (ibid.: 7).

The Colloque went on to discuss the following issues:

- (1) The endogenous reasons for the decline of liberalism (with Wilhelm Röpke giving the opening statement and identifying market concentration and limited liability as such endogenous reasons),
- (2) liberalism and economic nationalism (with, again, Röpke setting the agenda by refuting all economic justifications of imperialism),
- (3) liberalism and the social question (with Jacques Rueff identifying price-fixing and market interventions as major causes of social misery), and
- (4) exogenous (psychological) reasons for liberalism’s decline (with Alexander Rüstow blaming capitalism and industrialisation for alienating the people and leading to soulless mass-societies).

During the Paris discussions only one year before the outbreak of World War II, the brave rest of liberals was surely united in its rejection of totalitarianism. But what is more noteworthy from today’s perspective is that most participants held old economic liberalism accountable for its own decline. The task, as they saw it, was to safeguard ethical values such as individual dignity, liberty and responsibility, inter-individual justice and global peace. To defend these “old” classical liberal values, a “new” political programme and economic order – a new definition of state-market-relations – was deemed necessary.

I will try to sketch some basic aspects of this “new order” in due course. To end my account of the historical roots of “neo-liberalism” and to highlight the irony of history displayed in today’s attacks on neo-liberalism from proponents of both left and right let me quote from the final session of the Colloque. The term “neo-liberalism” was not undisputed. Some participants wanted to make more explicit exactly what it was that was “neo”. Proposals ranged from “libéralisme positif” (since “old” liberalism would too readily content itself with “negative” denotations of individual rights) to “libéralisme sociale” (since the benefits of a free society would far better serve social goals than those of socialist planning). Jacques Rueff offered his view by naming it “liberal politics of the left, because it tends to give the least advantaged classes the

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<sup>1</sup> All following quotes from the discussions of the “Colloque” are translated from the French publication that the author intends to soon publish in English. See also Plickert (2008) for an account of the Colloque and the ensuing development of various strands of neo-liberalism until today.

most well-being possible” (ibid.: 101)!<sup>2</sup> So much about the historical, profoundly European, roots of neo-liberalism.

### 3. Open market, strong state: the neo-/ordo-liberal view

The “Colloque” did, in the end, produce something like a neo-liberal agenda, which however, as a consensus-longing paper (written by Walter Lippmann), clearly had to be less controversial and substantial than the discourse that preceded it (ibid.: 99-101). A much more concise neo-liberal programme was meanwhile being developed, as a more or less openly anti-totalitarian plot, in Germany.

Members of the Freiburg School of Law and Economics had begun in the earlier 1930s and even more so during the Nazi regime (in various resistance circles<sup>3</sup>) to develop principles of a “workable and humane order” (Eucken 1952/1990: 14) of society that later became known as “*ordo-liberalism*” – an economic, legal and moral programme that would, after the collapse of Nazi-Germany, provide major inspirations for the German “economic miracle” based on an economic constitution labelled “social market economy”<sup>4</sup>. The two exiled German attendants of the “Colloque” – Röpke and Rüstow, who during their life-times had no problem to call themselves “neo-liberals” – had a comparable impact on the policies of Ludwig Erhard, the political entrepreneur who pushed through free prices and competition at a time when such policies were deemed extremely daring. Röpke, Rüstow and Erhard shared views very similar to those of Walter Eucken and Franz Böhm, founders of the Freiburg School. From a history of ideas perspective, it is certainly fascinating to mark and highlight methodological and political differences among different authors. But regarding fundamental ideas, and compared with the general trend of thinking at the time, the neo-liberalism of Röpke and Rüstow and the ordo-liberalism of the Freiburg School can reasonably be viewed as ventures of a common cause.<sup>5</sup>

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<sup>2</sup> In response to Rueff’s proposal, one participant (Louis Marlio) argued that the party-political dimensions of “right” or “left” were of no use in locating (neo-)liberal positions (Colloque Lippmann 1938: 102). Collectivism vs. individualism would be much more adequate criteria. Hayek’s contributions to the Colloque were only rarely kept due to the fact that only French and German interventions were recorded by dactylography and Hayek’s English statements had to be reconstructed from memory. One can imagine, however, that he would have sided with Marlio. His famous “Road to Serfdom” (Hayek 1944) was, after all, dedicated “[t]o the socialists in all parties”.

<sup>3</sup> See Goldschmidt (2005) for more details.

<sup>4</sup> See Goldschmidt/Wohlgemuth (2008a) on the theoretical sources of the German concept of a “Social Market Economy”.

<sup>5</sup> See Peacock/Willgerodt (1989) or Goldschmidt/Wohlgemuth (2008b) for collections and interpretations of original texts of the authors just mentioned. Indeed, their common cause is not identical in all details of defining a “just” order nor is the argument put forward with identical methodological means. One can distinguish rather romantic-conservative humanistic ideals developed within a broad sociological framework by Rüstow and Röpke from the rather pragmatic political demands that Eucken or Böhm based on economic systems analysis combined with the interdependent legal and political orders needed to ensure a workable and just social order (see Renner 2002). Differences between Hayek’s more Humeian evolutionary approach and Eucken’s more Kantian constructivistic approach can only be hinted at in this paper (see Streit/Wohlge-

Their common cause was to establish order – an economic and legal order that serves in the first instance not economic efficiency but rather individual liberty and social inclusion. Eucken and Böhm identified the “new social question” as that of unequal market power based on privileges of powerful economic groups with special access to state power. The old laissez-faire liberalism, they argued, had created a situation where cartels and monopolies (tolerated or even supported by state agencies) were exercising unwarranted and unjust power over consumers and potential competitors. A new liberalism would have to be one in which such power-relations based on privileges had to be dismantled. In other words, and as echoed in the Colloque’s session on the endogenous reasons for the decline of liberalism (Colloque Lippmann 1938: 25-45), a free market economy cannot in and of itself create its own ethical and institutional preconditions; it tends to become a closed circle for the powerful privileged instead of an open opportunity for the industrious individual.

Hence the call for a “strong state” (Eucken 1932: 319). Its strength was not to be derived from interventionist powers or a paternalistic, all-embracing care for the economy and society at large. Quite to the contrary, the “strong state” envisioned by the Freiburg “neo-liberals” gains its strength rather through self-restraint, through its ability to say “no” to the demands of special interest groups, its ability to credibly commit itself to universal moral principles of the rule of law enshrined in a privilege-free economic constitution. I shall come back to the role of the state which according to neo-liberals was mainly to enforce fair and equal rules of just behaviour which in the economic realm meant rules that allow open competition to unfold. But why was competition so important? What is its virtue?

#### **4. The ethics of competition**

It is very clear that for the ordo-liberals of the Freiburg School (as well as their neo-liberal friends such as Röpke, Müller-Armack or Erhard), competition was an essential tool to be used for social and ethical purposes, namely the benefit of the large masses of consumers via the emasculation of private power of producers. In order to discuss the ethics of competition in a more systematic and broader, but still rather rough, framework it might for the present purpose be useful to distinguish three to four dimensions of ethical judgements: Ethical praise as attributed to (1a) good intentions (deontological ethics), (1b) virtuous behaviour (virtue ethics), (2) just, law-abiding behaviour according to universalisable rules of just conduct or (3) desirable results (consequentialism). Good will, virtue, justice, and welfare may be categories roughly corresponding to these dimensions. I am certainly oversimplifying moral philosophy and ethics to a degree that reflects the limits of both my competence and the purpose of this paper (which is to broadly illustrate some ethical standpoints of some neo-liberal thinkers). Since I am here mainly concerned with social institutions and practices, differences between deontological and virtue ethics do not seem to me as rele-

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ment 2000 for more details). Mises, as already the documentation of the Colloque reveals, differs from all other protagonists mentioned here (including his student Hayek) by basing an uncompromising anti-statist view on an aprioristic logic. Mises clearly is the “odd man out” and thus shall not be counted amongst the original “neo-liberal” views presented here.

vant here. The point I try to make here is that a neo-liberal view of the “ethics of competition” relates to all ethical dimensions mentioned above, but it stresses an “institutional ethics” or “rights-egalitarianism” that relies on commonly acceptable rules that tend, overall, to enable and reward virtuous behavior and produce desirable social consequences.<sup>6</sup>

#### 4.1 Competition and virtue, justice or welfare

What made economics (and the classical liberalism that developed along with it) to be commonly regarded as a somewhat “immoral”, “dismal” science<sup>7</sup> was its reluctance to put much faith in and emphasis on the first criteria named above: good intentions or benevolence<sup>8</sup>. To be sure, economics as a social science started with Adam Smith (1759/1982) and thus with “moral sentiments” both as empirical facts to be taken into account in positive analysis and as praiseworthy demands in a normative context. But, as economists discovered then and would in principle maintain until today, good intentions, benevolence or virtue alone could neither guarantee justice nor welfare in an extensive order of coordination within large groups composed mainly of unknown, invisible, strangers. Here, it could only be an “invisible hand”, the incentive structure of competitive selection led by abstract rules of procedural justice (the second criterion), which made it possible that no recourse to benevolence was needed for an open market economy to yield desirable results or welfare (the third criterion) for multitudes of unknown others.

This general logic was expressed in the immortal quote of Adam Smith (1776/1976: 26f.):

“[E]very individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it (...) [B]y directing [his] industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention (...) By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it.”

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<sup>6</sup> This view has also been labelled “Ordnungsethik” (e.g. Homann/Kirchner 1995). For a political-philosophical way to lay a foundation of liberalism in “egalitarian human rights” and their expression in universalisable rules of just conduct, see Kersting (2004, 2006). For a defence of “individual ethics” based on internalized moral values or self chosen internal norms (1a and 1b above) and a critique of (purely) incentive-oriented “institutional ethics” (2 above), see e.g. Weise (2000).

<sup>7</sup> Another irony of intellectual history is that the branding of economics as the „dismal science“ originated from Thomas Carlyle, who, in a text on the “Negro question” published in 1849, attacked classical liberal economists for their anti-slavery standpoints and for a market egalitarianism that denied common notions of superior races or classes in society. Also Charles Dickens contributed to the bad image of economics and capitalism derived from a similar paternalistic and elitist standpoint (see Levy 2001).

<sup>8</sup> As in the case of Mandeville (1732/1998), even commonly proclaimed virtues were not necessarily endorsed if it could be shown that private vices could lead to public benefits.

It is well known that, already in Smith's system the desirable social *results* of self-regarding *intentions* depended, especially in a large society, on the invisible hand's being held by a visible arm of the rule of law, i.e. on market behaviour framed by commonly accepted *rules* of just behaviour (e.g. Homann 2006: 6f.). The latter aspect has indeed been disregarded within economics for too long.

Neo-classical economists in the early 20<sup>th</sup> century tried hard to (dis-)prove what they took for Smith's claim of the invisible but beneficial hand. However, with the tools of modern price theory and welfare-economics, it could be shown that only under impossible assumptions insuperable collective welfare results could be derived from "perfect competition". This ideal-type affords, amongst other technicalities, that there are countless, and still representative, omniscient actors both on the demand side and the supply side of a market for homogenous goods. Perhaps some of the disgust many intellectuals today feel towards "neo-liberalism" can be attributed to their having been exposed only to the most rudimentary – and rudest – textbook-versions of "neo-classical" economics and the perfectly unreal model of perfect competition. But most original neo-liberals' views on the virtue of competition were developed either before or in explicit opposition to the neo-classical construct of "perfect" competition as a paradigmatic benchmark of social welfare (see e.g. Kirzner 1994).

By discarding the fact of individual ignorance and by abstracting from social institutions, economics offered a scapegoat that was all too easy to either discard as useless or to use as an alibi for interventionist corrections of all too obvious real market failure (if compared to the economists' Nirvana). By disregarding both human condition and socially devised constraints to human actions, orthodox neo-classical economics also bid farewell to any useful discourse on practical ethics. The game of utilitarian calculus played amongst armchair economists who would move representative actors equipped with given knowledge, goods and preferences on an imaginary drilling ground of welfare functions is of neither practical nor moral significance.<sup>9</sup>

Already for the "classical-liberal" Adam Smith, and then again for the "neo-liberal" thinkers of the 1930s, it was not the "unfettered market" or "competition" as such that miraculously transformed even wicked intentions into socially beneficial outcomes. Rather, it was the second ethical criterion – justice of behaviour according to universal rules – that was a necessary condition for competition to provide commonly desirable results. And justice of behaviour towards unknown others had to become a matter of equality before the law. "*Liberté, Égalité, Fraternité*": the battle-cry of the French Revolution demarks a magic triangle of ethics to which liberalism (old or new) offers no simplistic catch-all answer – for good reasons.

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<sup>9</sup> See Zelizer (2007: 11): "views of the economy as an autonomous, distinctive sphere of human activity organized around rationality and efficiency have impeded the serious consideration of morality's place in economic life". See also Kersting (2006: 39ff.) on the limited (but still useful) value of using "homo oeconomicus" as a "worst-case scenario" for a prudent constitutional calculus, but as an impossible candidate for a justification of morality as such. Kersting argues that the morals of just cooperation only work within a context of moral understandings that, in cases of conflict, value morality higher than instrumental rationality. Even if an interest in reciprocal morality can be assumed, morality itself cannot be based in interest: "Wir können Moral nicht in Interesse fundieren, wir können aber ein Interesse an der Moral nehmen" (ibid.: 43).



Only within the natural bonds of the small group (brothers and sisters, family and friends) can “fraternity” (or benevolence, or virtue) be exerted by oneself and expected from others<sup>10</sup>. In order to remain “virtuous”, benevolence or solidarity must be voluntary. As Adam Smith (1759/1982: 78f.) notes in his work on “moral sentiments”: “benevolence is always free, it cannot be extorted by force”; and: “[t]here is, however, another virtue (...) which may be extorted by force (...) This virtue is justice”. And it is here that equality has its proper place and can be extended to anonymous societies. Equality is a necessary attribute of justice (and the law) only if it means equal demands on just behaviour of everyone. This includes “equal rights” and precludes “equal results” (equal distribution of income or of power) as criteria of justice (Hayek 1976: 67ff.). “Liberty” thus means both the prerequisite of unforced (thus virtuous) fraternity and the consequence of legally enforceable (thus just) equality before the law. And competition according to rules of just behaviour would become a morally justified demand of intended equality (before the law) with unintended results of benevolence (after the fact).

In order to substantiate this claim in a more structured way, I now discuss three possible ethical vindications of competition, all of which are interlinked and overlapping for good reasons in most “neo-liberal” arguments: Competition as a result and expression of individual liberty and private autonomy (*liberté*), competition as a result and a cause of the emasculation of privileged (market) power (*égalité*), and competition as a source of unintended good works for unknown others (*fraternité*).

#### 4.2 Competition as a result of equal liberty

In a most fundamental liberal, even natural-liberty-based, justification, competition can be based on equal liberty. Frédéric Bastiat, in his essay on “Economic Harmonies” (Bastiat 1850/1996: ch. 10.8) claims that although competition “is often harsh in its operation, there is no law that is richer in social harmonies”. To identify competition with harmony is certainly a challenging statement that not many of Bastiat’s contemporary compatriots would dare to make. But for him competition is simply a result of “the absence of oppression” and hence the most natural expression of freedom, of the “possibility of choosing, of judging, of comparing” (ibid.: ch. 10.4). This shows that the framing of academic discourse or, for that matter, public opinion polls on the merits of competition is crucial. Answers critically depend on the alternative that is being offered or insinuated: competition vs. oppression/monopoly/privilege or competition vs. cooperation/solidarity. I guess that the same people who would in abstract terms prefer cooperation to rivalry would also prefer competition to monopoly, open calls for papers and invitations for tenders to nepotism, competitive sports to “fixed” games or, for that matter, democracy to autocracy.

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<sup>10</sup> There are some famous exceptions to this rule of an inverse relation between effective fraternity, solidarity or love (*caritas*) and the size and anonymity of those to which these noble feelings are intended to apply. Mahatma Ghandi, e.g., did succeed in implementing an ethical approach among many people for some time. A really effective relief from poverty for the masses in India and the growing chances to determine their own way of pursuing happiness, however, might have more to do with the unintended emergence of “globalisation” or with the mutually beneficial “business model” of granting micro-credits to the poor.

Competition in the Bastiat-frame would not only be the most natural consequence of scarce resources and rewards (see Mises 1949/1966: 273ff.), it could also be regarded a most natural expression of freedom (which I would count amongst ethical social values) – and freedom more for those who are able to choose and compare than for those who are, by command of the choosers, “forced” to produce at profit. Competition serves the needs of consumers much more than the interests of producers. This has been the battle cry already of 18<sup>th</sup> and 19<sup>th</sup> centuries’ liberals: Get rid of the feudal and mercantilist privileges! Oppression of competition means barred market entry, cartels, monopoly (often enough created or protected by the state). Oppression of competition means oppression of individuals’ equal freedom to exercise their talents and pursue their own goals by using their own, personal, knowledge.

Other than Bastiat, but also Hayek (1960) or Friedman/Friedman (1981), Amartya Sen has never been content with an exclusively “negative” definition of freedom from coercion or freedom to choose. He endorses a much wider notion of “freedoms” that would also include positive, material, notions of capability to act and “freedom to achieve” (Sen 1994: 125). This is not the place to go into the details of Sen’s various definitions of “positive liberties” as “capabilities” (e.g. Sen 1993). But his claim that “we have to go well beyond the space of utilities – and beyond ‘efficiency’ in that space – to assess the market-mechanism” (Sen 1994: 124) is quite in line with the (historically correct) “neo-liberal” or “ordo-liberal” attitude and it is similarly distanced from Chicago-style or Misesian, economic or a-priori, foundations of most forms of “neo”-libertarianism. But note that Sen’s own assessment of market-competition leads him to claim that it is at least “weakly efficient in terms of achievement-freedoms” (ibid.: 130).

Indeed, any kind of “strong efficiency proof” in terms of achieved welfare can only be provided by ways of all-too-strong assumptions that are never “reality-proof”. Some aspects of the model of “perfect competition” have already been rejected above as obsolete for a neo-liberal argument and they were, in fact, fiercely rejected by original neo-liberals. Especially the assumption of “given” and “complete” information of market actors contradicts the later developed neo-liberal vindication of competition as a “discovery procedure” (Hayek 1968/1978), which only makes sense under conditions of imperfect and scattered information that can be made socially beneficial only under conditions of free price-formation in a competitive market-process.

However, as soon as the neoclassical assumption of “representative actors” is also rightfully dropped, one of the things to be discovered by competition is that under rules of equal negative freedom to choose unequal results for unequally lucky and able market participants necessarily and drastically emerge. Thus, competition as such provides little comfort for the fact that “the disabled, the old, or the handicapped may have, on the one hand, more difficulty in being able to get a good job and to earn a decent income, and on the other, also to face greater difficulties in converting incomes into capabilities to live well” (Sen 1994: 131). Indeed, free competition only relies on equal chances in the sense of equal (negative) freedom for all to try and transform their efforts into personal well-being. It thus also tends to transform unequal capabilities into unequal chances to succeed in the sense of “positive freedoms” to achieve nearly as much as the more capable or lucky others.

The “weak efficiency” of a competitive order thus cannot in any way provide equally positive freedom and well-being for all. This is its primary weakness, but also its strength; since without free competition, there should be less available remedies for unfortunate distress, as the following two chapters try to show. The comparatively strong inefficiency (and often injustice) of monopolies and cartels should even be worse for the handicapped poor<sup>11</sup>. This is why neo-liberals seek to find solutions to obvious hardships not through interfering with the price-mechanism or curtailing competition. Rather, the causes of social distress had to be addressed by ways of unprivileged access to primary basic goods such as education, health care and entrepreneurial activity (similar opportunities)<sup>12</sup>. And the effects of remaining inability to earn market incomes and enjoy a humane standard of living had to be addressed by direct transfers of services and/or money to those in need instead of measures aimed at distorting the competitive price-mechanism.<sup>13</sup> No serious qualification of equal (negative) freedom to compete has to arise from social insurance schemes equally applicable to all.

### 4.3 Competition and the emasculation of unsocial power

“Equal freedom” or the “denial of all privilege”<sup>14</sup> can be seen as primary ethical demands – with competition, the equal opportunity to access markets, being a most natural consequence. At the same time, competition can be ethically valuable not only as a consequence of ethical standards and rules of procedural justice, but also by virtue of its (unintended) consequences. The two aspects – moral/ethical “input” and moral/ethical “output” – are often hard to distinguish. This is especially true for the neo-/ordo-liberal view of competition as an answer to the “social question”. Neo- or ordo-liberals considered (not only: but all too often state-protected) cartels and monopolies to be the major source of the “new social question” (Eucken 1951: 56 ff.), because such artificial prevention of open competition tended to deprive not only

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<sup>11</sup> See Eucken (1951: 63) who notes that “distribution can be particularly unequal and unjust where economic power is concentrated and, besides, bound up with administrative power”.

<sup>12</sup> The Rawlsian tone is quite intended. One of the many interpretations of his famous “Theory of Justice” (Rawls 1971) could also be somewhat “neo-liberal” (see, e.g. Karsten 1985). Even Hayek (1976: xiii) argues that “we agree on what is to me the essential point”, and refers to the following quote by Rawls (1963: 102): “the principles of justice define the crucial constraints which institutions and joint activities must satisfy (...) If these constraints are satisfied, the resulting distribution, whatever it is, may be accepted as just (or at least not unjust).”

<sup>13</sup> This is not the place to discuss the major contractarian justifications of even compulsory social insurance schemes as proposed e.g. by Hayek (1960: ch. 19), Vanberg (2005/2008) or Rawls (1971). In all these concepts, equal freedom to compete is seen as a necessary condition for promoting the wealth of the greatest numbers, but not a sufficient condition for avoiding social hardships of the handicapped or very unlucky. Thus, a liberal society is well-advised to insure all of its members against the risks of severe hardships and to provide a minimum income and maximum dignity for the least advantaged.

<sup>14</sup> See Hayek (1972: ix): “The essence of the liberal position (...) is the denial of all privilege, if privilege is understood in its proper and original meaning of the State granting and protecting rights to some which are not available on equal terms to others.”

potential rival producers, but also consumers and workers of viable alternatives to the conditions dictated by the privileged and powerful few.

Thus, if Eucken (1951: 40) claims that the “problem of power is the obverse aspect of the problem of freedom” and that the “*Wettbewerbsordnung*” (order of rules enforcing open competition) is the key to solving both problems simultaneously, he has in mind several interrelations between competition, power and freedom: (a) Unlimited freedom does not lead to open competition, but becomes a major source of power and privilege<sup>15</sup>. (b) Legal privilege breeds economic power and economic power breeds political privilege; both tend to violate equal freedom as well as open competition. (c) Competitive market entry and rivalry tends to contest and reduce socially harmful positions of market power; thus: (d) Universalisable rules that define fair and equal rights of market-behaviour tend to simultaneously ease the problem of self-destructive freedom and the problem of self-preserving power positions.

In short: the main moral “output” the ordo-liberals were focussing on was the increase of individual autonomy and liberty as a result of the “emasculatation of power” created by competition enforced by the rule of law. In this sense, Böhm (1971/2008: 306, my translation) argued: “the great importance of competition is by no means just that of an incentive-mechanism, but rather that of an instrument to abolish power (...) [N]ot only the level of performance and growth, (...) but also the substance of freedom, equilibrium and justice of the market system depends on competition.” In Böhm’s quote as well as in views commonly held amongst intellectuals or politicians “performance and growth” seem rather secondary candidates for ethical praise compared to “freedom and justice”. Behind these economic “incentive mechanisms” and the material goods they help create, one can, however, in a system based on market competition, discover one very peculiar moral good: unintended altruism.

#### 4.4 Competition and unintended altruism

The beneficial material consequences of a market economy based on both open market access and universalisable rules of just conduct have already been alluded to. And indeed, they are not only a recurrent finding of the latest empirical cross-country findings over time.<sup>16</sup> They have already been the essential part of Scottish moral philosophy informed by basic economics in the 18<sup>th</sup> century. *Neo*-liberals such as most of those assembled at the Colloque Lippmann did not attack classical liberalism because of its claim that competitive markets would indeed lead to the best possible provision of consumer goods – from essential nutrition needed to feed an enormously growing population to things that first were luxury goods for a fanciful few and soon became objects of mass-production catering for popular demand. Neo-liberals and all other sorts of intellectuals rather became disillusioned about 19<sup>th</sup> and 20<sup>th</sup> century forms of what also Marxians decried as “state-monopoly capitalism” in which privi-

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<sup>15</sup> The standard example used by the ordo-liberals was the vindication of cartel-arrangements based on the principle of “freedom to contract” which historically were even given legal protection by German courts. Such contracts to the detriment of third parties create market power and infringe on the freedom of others to compete (see Eucken 1951: 31f.).

<sup>16</sup> See, e.g. the data-series in “Economic Freedom in the World” (Heritage Foundation 2008).

leges were granted by the state to powerful captains of industry and in which cartel-arrangements were given legal licence and political support.

As soon as such state protection of powerful industrialists and interest-groups would be abandoned, most neo-liberals might have been ready to re-embrace the “old”, classical-liberal view as has been vigorously expressed, e.g., by Hayek<sup>17</sup> in his refined consequentialist argument: “The morals of the market do lead us to benefit others, not by our intending to do so, but by making us act in a manner which will, nevertheless have just that effect. Our ‘altruism’, in this new sense, is very different from instinctual altruism. No longer the end pursued but the rules observed make the action good or bad” (Hayek 1988: 81). This unintended altruism triggered by rules and incentives is both a cause and an effect of the growth of society once it turned from the naturally closed society of hunter-gatherer tribes (or the artificially closed society of central planning) to the “extended order” (Hayek 1988: 38ff.) or “open society” (Popper 1945/1966): “It did become the ethos of the Open Society that it was better to invest one’s fortune (...) to cater for the needs of thousands of unknown people rather than to provide for the needs of a few known neighbours” (Hayek 1976: 145).

This is not a minor social achievement. At the same time, it has always been a source of moral indignation. After all, intrinsically moral aspects of the particular needs themselves are no essential part of the “catering”. In a competitive market economy, Adam Smith (1776/1976: 660) found, “it is perfectly self-evident” that “consumption is the sole end and purpose of production”. What is being consumed for what reasons by whom is of little concern for competing producers. Their “altruism”, thus, is not only unintended, it is also un-paternalistic as it does not judge the ethical value of the wants that are satisfied. This has led Frank Knight (1922: 580) to argue that, from an ethical standpoint, “we cannot accept want-satisfaction as a final criterion of value” and we cannot evade an ethical evaluation based on a “desire for wants of the ‘right’ kind”. Knight’s deontological standard of ethics based on the “character of the motive which led to the action” (ibid.: 621) or the “Christian ideal of spiritual friendship” (ibid.: 622) does indeed provide no ethical justification of competition, narrowly defined as an anonymous mechanism of non-discriminating want-satisfaction. Competition in that regard is at best ethically neutral; although it is derived from the same liberal principles which leave self-directed individuals free to choose amongst alternative lives, without which, according to Knight, “there is no such thing as ethics”.<sup>18</sup>

The individual ethics of having the “right” wants has to be created and promoted “beyond the realm of supply and demand”, as forcefully argued also by the neo-liberal Wilhelm Röpke (1958). In a similar vein, and rightly distinguishing levels of appropri-

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<sup>17</sup> Even more vigorous were, of course, the rather libertarian views of Ludwig von Mises (1927/2005) and his followers such as Rothbard (1970). By regarding the state not as a potential facilitator, but as a natural enemy of freedom and justice, they should not (and would not have wanted to) be counted amongst the proponents of a neo- or ordo-liberal agenda.

<sup>18</sup> See Knight (1922: 618): “Ethics deals with the problem of choosing between different kinds of life, and assumes that there is real choice between different kinds, or else there is no such thing as ethics. The ethical character of competition is not decided by the fact that it stimulates a greater amount of activity; this merely raises the question of the ethical quality of what is done or of the motive itself.”

ate supply of different kinds of morals, H.B Acton (1993: 12) states: “Competitive capitalism, then, gives scope for self-directed individuals to set up and keep production going. What is produced depends upon what the consumers want. What they want depends upon how well they have been brought up. If they have been well brought up, their patterns of demand will be morally acceptable. If they have been badly brought up, their patterns of demand will be morally unacceptable”. In short, the market is no substitute for moral education. But competitive capitalism, if justly framed by adequate rules, provides strong incentives to learn at least that one can best benefit oneself by benefiting others (see e.g. Baumann 1996).

## 5. The “competitive order” and the state

As argued above, a neo-liberal “ethos” of competition with its consequences of unintended but enormous benefits was primarily based on general rules of just behaviour. Without such common rules neither commonly accepted behaviour nor commonly desired results of competition can be expected to emerge spontaneously. This is the core conviction of “classical neo-liberals”. However, with the transition towards the “Open Society”, the standards of justice had to become more abstract and, in a sense, more loose in order to reflect the increasing numbers of those who would be able and willing to adhere to these rules – and in order to produce the ever more unlimited effect of unintended altruism granted to strangers: “the new morals of the Open Society (...) not only indefinitely extended the circle of other people in relation to whom one had to obey moral rules, but (...) this expansion of the scope of the moral code necessarily brought with itself a reduction of its content” (Hayek 1976: 146).

The “Open Society” has never been regarded as a natural, anarchic phenomenon. Its very existence and its beneficial social consequences depend on clearly defined property rights (including obligations such as liability) and institutions, that is: commonly shared rules and procedures enforced by a credible threat of sanctions for those who expect an advantage by breaking the rules. As an enforcement-mechanism the nation-state with its almost “natural monopoly” (Wohlgemuth 2000) of ideally legitimate coercion has for a few centuries been the strongest candidate if the “Open Society” was to be defended against its “enemies” (Popper 1945/1966). But at the same time, historically, “the role of the state was at best ambiguous, because the state was as often an increasing source of insecurity and higher transaction costs as it was protector and enforcer of property rights” (North 1990: 35).

Thus, when it comes to state-market (or more broadly: state-society) relations, the common “neo-liberal” view is that the state would and should be able to enforce exactly those rules that a private-law-society might, in principle, be able to “culturally” develop on its own, but that could be more efficiently and equitably enforced by a third party with enough strength (based on increasing returns to scale) and enough distance (based on its not being a market actor itself) to do the job.<sup>19</sup> The whole

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<sup>19</sup> It would unduly prolong this paper if I were to discuss all neo-liberal or classical liberal assertions of this claim. On the relation between a “private law society” and a protective state, see e.g. Böhm (1966/1989). Between traditional ordo-liberalism and the later rejuvenation of the “Freiburg School” after Hayek brought less static and statist ideas to Freiburg, Böhm’s work pro-

question of state-market relations thus depends on the trust that one can have in the state's ability to enforce universalisable rules of just behaviour. The answer, in turn, depends on how politicians administering the natural monopoly of coercion can credibly commit *themselves* to rules governing their *own* behaviour. Such rules are manifold and may be crudely summarised under two headings: democracy and the rule of law. Modern neo-liberals believe in both as long as they serve, in combination, to lead political authorities to act as agents of their principals (the citizens) in their (the citizens') pursuit of realising "gains from joint commitment" (Vanberg 2005: 27) which private initiatives would often fail to realise.

Both democracy and the rule of law – and the combination of the two – seem to be the most particular "cultural" achievements that Europe, during many centuries of disastrously testing the opposites, has produced. Markets (and thus consumers and entrepreneurs) have prospered mostly in times when leaders of the state were able to live up to their credible commitment to the rule of law protecting private property and free competition – quite often against their own short-term political self-interest. The very incentive for such a socially beneficial commitment was itself the product of political competition! Such political competition can, again, take two civilised forms: democracy or federalism (within nation states) and/or inter-jurisdictional competition (between nation states). Historically, it has been the latter – competition between jurisdictions trying to offer more hospitable conditions for private enterprise – that has been a major source of economic wealth – especially on the European continent. In addition, this competition amongst innumerable European principalities also rewarded jurisdictions that were able to credibly commit themselves to constitutional provisions providing both democracy and the rule of law<sup>20</sup>.

## 6. Neo-liberalism and the construction of Europe

The idea that the *nation*-state was to be the sole best guardian of a neo-liberal "*Wettbewerbsordnung*" was challenged very soon after WW II and with the first attempts to create a European Economic Community (EEC). Influential neo-liberals were at that time – the mid 1950s – mostly Germans. An EEC of only six states from the free "West", and inspired, as it must have seemed at the time, by French desires for comprehensive (supra-)state-interventionism, was for neo-liberals (such as the German Minister of Economic Affairs, Ludwig Erhard, and his most outspoken advisor, Wilhelm Röpke) an imminent threat to their aspirations both nationally and internationally. This is not the place to retrace the delicate situation and the ardent debates of that time<sup>21</sup>. But little over 50 years after the Treaty of Rome was signed, some prelimi-

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vides a very useful link (see Streit/Wohlgemuth 2000). Böhm had two advantages: he lived much longer than, e.g., Eucken; and he was a legal scholar, not an economist. Thus, he was able to develop a broad view of neo-liberal legal philosophy without being distracted by ephemeral fashions of neo-classical economic modeling.

<sup>20</sup> On the intellectual legacy of and empirical advocacy for "institutional competition" in which citizens can satisfy their political preferences by ways of "exit", see the manifold sources in Vaubel (2008).

<sup>21</sup> See Wohlgemuth (2008a) for a more detailed account of the early stages of European integration and the partly frustrated hopes and partly refuted fears of neo-liberals.

nary conclusions of the effect of neo-liberalism (in the historical and not in the polemic sense) on the construction of Europe seem possible.

Germany has not only been the European “export champion” in terms of goods and services (for most of the last 50 years). Her most precious institutional “goods and services” of older, neo-liberal days, have meanwhile been “Europeanised” to a stunning degree: stable currency, free trade, and “unfettered competition”. All these policy-fields have, meanwhile, been completely or largely “outsourced” to the European Central Bank, the European Commission or European Court of Justice. By being more effectively protected from the demands of national special interests and the logic of pleasing minority-coalitions in order to overcome re-election constraints, these agencies have often been able to defend “neo-liberal” principles more effectively than national governments would have been able to.

At the same time, however, especially by ways of in-transparent log-rolling within the European Council and bureaucratic ambitions within the European Commission, European Courts, European Committees and the European Parliament, the EU has been a major producer of an “*acquis communautaire*” of interventions and regulations that often cannot be argued to be universally “just” or preferable by taking the increasing heterogeneity of individual opinions or interests into account (see Wohlgenuth/Brandt 2007, Alesina et. al 2001). When speculating about the political-economic “conditions of inter-state federalism” in Europe, Hayek (1939/1948) was remarkably enthusiastic about such a project, at a time when such hopes were certainly doomed. But, theoretically he had a point, and with the benefit of historical hindsight, he was partly proven right. Hayek argued that democratically organized nation states would find their mutual benefits of joint commitment mostly in the area of negative liberties: “securing peace” (ibid.: 255), the “free movement of men and capital” (ibid.: 258), reduced privileges and state-interventionism (ibid.: 262f.). In short: “in the international sphere, democratic government should only be possible if the tasks of the international government are limited to an essentially liberal program” (ibid.: 271).<sup>22</sup>

## 7. Outlook: Competing institutional variety as Europe’s “Social Model”

In this paper, I have tried to neither reproduce nor comment on the well known and heavily publicized discussion on “European Social Models”<sup>23</sup>. Instead, I wanted to outline just one candidate for a truly “European” model of state-market relations. The ironic twist is that the label which can with historical correctness be attached to it is also the momentarily most contested and even detested one in Europe: “neo-liberalism”. What I presented was neo-liberalism as “invented” 1938 in Paris during a conference of mostly European thinkers trying to prevent the fatal demise of European culture and liberty which occurred only one year later. And it was this neo- or

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<sup>22</sup> As argued in more detail elsewhere (Wohlgenuth 2008a), Hayek’s idealist neo-liberal reasoning might have been conceptually right; but he was quite naive concerning political tactics and the logic of log-rolling that produced some 90 000 pages of European legal provisions that involve quite a lot of mutually traded privileges.

<sup>23</sup> See Esping-Andersen (1990) for the most quoted trigger of the academic and political debate.



ordo-liberalism which after 1948 started as a “German Social Model” which produced the so-called “*Wirtschaftswunder*” that became envied all over Europe. And it is this neo-liberalism that found its way into the core of the Roman Treaties in 1957 (apart, obviously, from certain parts such as agricultural policy).

Thus in a certain, but limited sense, one could argue that neo-liberalism actually *was* a “European Social Model”. The universal rules of just conduct that guarantee free movement and open competition and prevent discriminatory state intervention have to some degree been successfully “Europeanised”. However, the European Union and its member states go far beyond the neo-liberal definitions of core state responsibilities. And those seeking to define a “European Social Model” mostly want the EU to go well beyond the completion of the internal market. They want labour market policies, welfare policies or tax policies to be further “harmonised” within the EU. In this way, “old Europe” may be trying to protect its paternalistic welfare-states which have come under stress from global competition.

Collectivist “social models” such as socialism and fascism were originally invented and tested in the very heart of Europe (and mostly in Germany) not too long ago. At the same time, Europe can historically claim to have been the often shaken cradle of a very fruitful offspring called “Western” civilisation – a legacy of Greek democracy and philosophy, Roman law and citizenship, Christian ethics, British Rule of Law, French and German enlightenment – however debatable such exclusive attributions may be from a historical perspective<sup>24</sup>. But such “shaking”, exploring, testing, adopting and rejecting, has, over many centuries, also shaped Europe and made it strong, innovative and exciting. It has been the competition amongst principalities, states, religions, schools of thought, and thus of laws, institutions, policies, social practices, that produced the “European miracle” (Jones 2003).

This “institutional competition” can work very much like market competition as a socially beneficial “discovery procedure” and learning process (Wohlgemuth 2008b). It is a most useful procedure once we acknowledge politicians’ and citizens’ constitutional lack of knowledge concerning present and future social problems and adequate political responses. In addition, decentralisation and inter-jurisdictional competition are the only ways to account for the fact that citizens have different and changing preferences also concerning the “social models” that they will have to finance and endure. Institutional competition is no equaliser or “ex post harmoniser”. It is a permanent process of creating, comparing and adopting different responses to different needs, capabilities, and preferences. Just like competition described here, also peaceful rivalry for best solutions amongst jurisdictions is the expression of equal liberty, it reduces (political) power, and is another beneficial source of progress and wealth (see also Rosenberg/Birdzell 1986).

The “ethics of competition” may historically have been a unique European “invention” – successfully exported some time ago to Northern America and increasingly adopted today in many parts of the globalised world. The irony of history may be that we Europeans are now trying to fend off global competition, our own invention that

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<sup>24</sup> See Nemo (2005) for a forcefully „Euro-centric“ definition of Western civilization and Nemo/Petitot (2007) for a comprehensive overview of the history of European liberalism.

made us grow and develop our own civilisation. The neo-liberal economist Wilhelm Röpke (1958: 365, my translation) was early aware of this danger:

“If we wanted to try to organise Europe in a centralist way (...) and forge it into a more or less closed block, this would mean nothing less than to betray Europe and the European patrimony. It would be an all the more malicious betrayal since it is committed in the name of Europe by ways of a disdainful abuse of its name.”

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