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## A COMPREHENSIVE STUDY ON LAISSEZ-FAIRE ECONOMICS

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### ABSTRACT

*This Study Is To Show That How The Idea Of Laissez-Faire Worked Out Through The Course Of History. How It Has Been Reshaped And Reformed. How The Simple Thoughts Go To Make A Difference In Socio-Political And Economic Fabric Of The Society In A Big Way. This Paper Traces Contributions And Developments Made To The Idea Of Laissez-Faire Right From Its Birth To The Current Times To Show How It Eventually Survived In The Garb Of Welfare Economics.*

**Key Words:** Laissez-faire, Welfare Economics, Economic Development

### INTRODUCTION

It is simplistic to say that attempts to understand capitalism began with Adam Smith. Capitalism as the dominant social, political and economic system first of Western Europe and later much of the world, emerged very slowly over a period of several centuries. One of the defining features of capitalism is private ownership of the means of the production. This means that society grants to private persons the right to dictate how the raw materials, tools, machinery and buildings necessary for the production can be used. Such a right necessarily implies that other individuals are excluded from having any say about how these means of production can be used. Another defining feature of capitalism is that most people are motivated by individualistic, acquisitive, maximizing behavior. This is necessary for the successful functioning of capitalism. First, in order to assure an adequate supply of labor and to facilitate the strict control of workers, it is necessary that working people produce commodities whose value is far in excess of the value of the commodities that they consume. In the earliest period of capitalism workers were paid such low wages that they and their families were kept on the verge of extreme material and social deprivation. As capitalism evolved the productivity of workers increased. They began to organize themselves collectively into unions and workingmen's associations to fight for higher wages. By the late nineteenth and early twentieth centuries, after many hard battles and innumerable setbacks, these struggles have an impact since that time, the purchasing power of the wages of working people has been slowly and consistently increasing in place of widespread physical deprivation, capitalism has increasingly had to rely on new types of motivation to keep working people producing the social surplus. A new social ethos sometimes called consumerism, has become dominant and is characterized by the belief that more income alone always means more happiness. In order to trace the outlines of the historical evolution of capitalism, it is necessary first to say a few words about feudalism- the socioeconomic system that preceded capitalism in Western Europe. In western countries, we find a real emergence of economic thought in its dynamic form only in the wake of changing character of the economic and during the phase of a transition from feudalism to commercial



capitalism. To understand capitalism, we have to understand the basic tenet of Laissez-Faire which means complete freedom but before that, we will discuss how its genesis began. We will discuss the genesis of Laissez-faire from the early mercantilist writings. The philosophy of mercantilists was essentially that of materialism. They believed that economic factors could be controlled by human management and arrangement. They were optimistic about the perfectibility of man and the human power to cross over the limitations of the environment. This is clear from what Hobbes writes that Nature has made men so equal in the faculties of the body and mind that exists no great difference between one individual and the other. Locke, however, has recognized the importance of environmental influences. The second important factor upon which their philosophy was based was that of self-interest. They believed that man acted under the influence of the principle of least sacrifice and all his actions were motivated by self-interest. “Every man”, said Hobbes “is presumed to do all things in order to his own benefit”. According to Fortery, “interest more than reason commonly sways most men’s affections .....And the hope of gain commonly bears so great a sway amongst men that it alone is sufficient to prevail with most.” The Mercantilists regarded state as the supreme power for controlling the activities and regulating the life of its citizens. The state was the master and man its servant with their emphasis on nationalism of economic and physical resources for strengthening the state. They desired that all men should work under its guidance. Mercantilists thus believed that powerful states meant powerful nation. Alexander Gray has beautifully summed up the Mercantilist concept of states: “in all their schemes the Mercantilists looked to a benevolently paternal government assumed wise enough to interfere everywhere. Mercantilism was a policy of ubiquitous and perpetual governmental activity. There was nothing that Government might not do; there was nothing that ought not to do, if thereby its activity was calculated to promote the general well-being. The state policies, in those days, were naturally shaped according to their ideas. Acts were promulgated for the encouragement of tillage, various laws, such as the Corn Laws, navigation laws and laws for regulating the prices of bread were formed. During the times of Colbert in France, the state’s jurisdiction over manufacturing industry knew no limits. The state could dispose of the resources of manufacturers. It decided who should be allowed to work and what things should be produced, what material should be used and what processes be followed. Mercantilist theories and policies have been criticized by a host of writers. The opposition actually started towards the end of the 17<sup>th</sup> century. The decay of Mercantilism, in fact, began when some of the Mercantilist writers who were much liberal in their views, started decrying the policies adopted by Colbert’s in France and by the King of England. In England, William Petty, Locke and Dudley North were the chief among these writers. Petty advocated freedom of trade and demolished the entire structure of mercantilist theory of money and price. Locke put forward the advantages of individual liberty and challenged the basic assumptions of mercantilism. North was the most vehement, direct and tactful critic. He said that wealth did not consist of only gold and silver.

Mercantilism appeared again in the first quarter of the 20<sup>th</sup> century. Especially, after the First World War. It again became the guiding principle of state policies. Although the ideas in favor of a strong national government had already started reappearing in Germany, England, and other countries in the first half of the 19<sup>th</sup> century, they gained momentum only after the



thirties of the 20<sup>th</sup> century. The policies that were in vogue during 16<sup>th</sup> and 17<sup>th</sup> centuries reappeared with certain modifications and refinements. Various national governments started using them as the tools for solving the economic problems created by Laissez-Faire. Haney Lewis called it Neo-Mercantilism. There started a race between countries to extend their sphere of influence and trade to other countries, with the sole object of getting a control over their resources and acquiring the services of their people for colonizing, conquering and establishing colonial supremacy.

Physiocrats-a group of French thinkers evolved a system of economic thought which forms one of the important roots of the modern science. Quesnay- a leading physiocrat was a medical doctor and studied the economic system as if it were a natural organism. The equilibrium in which the economy naturally found itself was seen as a manifestation of the natural order of things. Here the influence of natural –law philosophy is apparent. Any man could appreciate the doctrine that his private business was no concern of government. It is natural that the crisp, sweeping exaggerations of the physiocrats system should have been very effective. The physiocrats were a scheme designed by God and therefore the regulatory hand of the state was not needed in its implementation. Since private property and the institutions of landowners was the basis of natural order, therefore, the first duty of the sovereign was to preserve this sacred institution “since liberty and property spring from the very nature of man and are necessary to his individualism, human laws should merely recognize, formulate and maintain them”<sup>1</sup>.

Adam Smith stands as an institution by himself in the history of economic thought, his contribution to the development of economic science cannot be over-estimated. The seeds of a very large number of later developments are found in his classic and voluminous book “an inquiry into the nature and causes of the wealth of nations” which was published in 1776, for a long period of time he was unanimously acclaimed as the true founder of economic science in spite of the originality and vigor displayed by the physiocrats before him. Adam Smith simply aimed at demonstrating that individuals serve the collective interest precisely because they are guided by self-interest. Intending only their own good, men are led by an invisible hand to further social ends. The underlying thesis is that the interest of the community is simply the sum of the interests of the members who compose it: each man if left alone, will seek to maximize his own wealth; therefore, all men, if unimpeded will maximize aggregate wealth. After Smith, there was a period of enthusiasm and optimism. It was that of Thomas Robert Malthus. And now a new kind of thought was arising which substantiated Laissez-Faire. It was that of utilitarianism- it was developed especially in Great Britain and which finally led to the work of Bentham as the belief spread that the economic agent is self-interested and competitive being, the idea also gained ground that all reasons for human action spring from the desire to obtain pleasure and avoid pain. This belief is the heart of utilitarianism whose normative formula is “the greatest happiness for the greatest number”. According to Bastiat, government performs its actions by the exercise of force, and there is only one place where it has, in his opinion, a moral right to exercise force. That is establishing justice. The action of Government is essentially limited to the maintenance of order, security and justice, all action of government beyond this limit is a usurpation upon

<sup>1</sup>Charles Gide and Charles Rist, A history of Economics doctrines (2<sup>nd</sup> edition) page, 68.



conscience, upon intelligence, upon industry; in a word upon human liberty, his doctrines appeared unduly warped by his propaganda against protectionism and socialism. Mill found himself in a society which was experiencing the fruits of the industrial revolution- both in terms of production potentials and in terms of stresses and strains, human and social problems and the manifestation of emerging economic conflicts. Mill argues for governments intervention and at the same time provides a discussion of limitations on it, his basic rule was that Laissez-Faire should be the general policy and any deviation from it should be considered on evil unless proved to be for the general good. The objective should always be the greatest good of the greatest number. As the 19<sup>th</sup> century began, the difficulties of extreme individualism and laissez-faire became apparent, not only in theory but also in dealing with the practical problems of crises, unemployment, poverty, monetary manipulation and war. The underlying assumptions of classicism have led either to pessimism or to a futile and unreal optimism. So socialists arose who have emphasized on greater equality in distribution and vehemently attacked Laissez-Faire policy and asked for abolishing private property, socialism either in the form of utopian or in state socialism or in the garb of scientific socialism all were pointing to the same fact that complete freedom can be prove detrimental. As they thought that because of free markets and complete non-intervention by the government, capitalist exploit the workers so government should step into protect the vulnerable section of the population from getting exploited. Because of socialism, a new concept arose “welfare economics”. Even now this type of economics exists. Nowhere we find Laissez-Faire being followed, the so-called capitalist economies follow welfare economics. Principles i.e. role of the government is to protect the people, maintain law and order, administer justice, provide merit goods and let the markets work on the principle of demand and supply forces. So to maintain the existence of Laissez-Faire, it was necessary to bring some changes in it so it could sustain the changing economic conditions. The debate around “Laissez-Faire” has given birth to so much economic literature that it encompasses every political thought. Even though Laissez Faire as propounded by Adam Smith is nowhere to be found in its original nature but this concept has withstood the vagaries of human behavior and time and still exists today but in its newer version i.e. “welfare Economics which can be called 21st century’s Laissez-Faire.”

### **EVOLUTION OF LAISSEZ- FAIRE**

Laissez-faire is an economic environment in which transactions between private parties are free from government restrictions, tariffs, and subsidies, with only enough regulations to protect property rights. The phrase laissez-faire is French and literally means "let [them] do". According to historical legend, the phrase stems from a meeting in about 1681 between the powerful French finance minister Jean-Baptiste Colbert and a group of French businessmen led by a certain M. Le Gendre. When the eager mercantilist minister asked how the French state could be of service to the merchants and help promote their commerce, Le Gendre replied simply "Laissez-nous faire" ("Let us be," literally "Let us do").<sup>2</sup>

The anecdote on the Colbert-Le Gendre meeting was related in a 1751 article in the *Journal economique* by the French minister and champion of free trade, René de



Voyer, Marquis d'Argenson – which happens to also be the phrase's first known appearance in print.<sup>3</sup> Argenson himself had used the phrase earlier (1736) in his own diaries, in a famous outburst and translated as:<sup>2</sup>

(Trans: "Let it be, that should be the motto of all public powers, as the world is civilized ... That we cannot grow except by lowering our neighbors is a detestable notion! Only malice and malignity of heart is satisfied with such a principle and our (national) interest is opposed to it. Let it be, for heaven's sake! Let it be!")

The laissez-faire slogan was popularized by Vincent de Gournay, a French Physiocrat who is said to have adopted the term from François Quesnay's writings in China<sup>4</sup>. It was Quesnay who coined the term laissez-faire, laissez-passer, and laissez-faire being a translation of the Chinese term Wu Wei. Gournay was an ardent proponent of the removal of restrictions on trade and the deregulation of the industry in France. Gournay was delighted by the Colbert-Le Gendre anecdote<sup>5</sup> and forged it into a larger maxim all his own: "Laissez-faire et laissez-passer" ('let do and let pass'). His motto has also been identified as the longer "Laissez-faire et laissez-passer, le monde va de lui même!" ("Let do and let pass, the world goes on by itself!"). Although Gournay left no written tracks on his economic policy ideas, he had an immense personal influence on his contemporaries, notably his fellow Physiocrats, who credit both the laissez-faire slogan and the doctrine to Gournay.

About the middle of the eighteenth century, a group of French thinkers evolved a system of economic thought which forms one of the most important roots of the modern science. It was a school of thought being based upon a belief in the existence of natural laws which must be followed if men are to gain their highest well-being. This system was also known as the "agricultural system" and is so called by Adam Smith. The physiocrats liked best to call themselves "The Economists" (les économistes).

The philosophy underlying the political economy of physiocrats was "natural order" and the law of nature. They believed in an ideal order of things, whose arrangements were perfect and whose laws were the will of God. This was the "ordre naturel". It stood opposed to the "ordre positif", whose laws are human and whose arrangements were imperfect ones. In their teachings, they sought to expound the principles of the ordrenaturel, that nation being best governed whose laws, or ordrepositif, come nearest to expressing the constitution of the natural order. The natural order of society, however, is not to be confused with the "state of nature". For it is founded upon law and property rights. The physiocrats, therefore, were far from adopting the conclusions of Rousseau. Doctor François Quesnay, who was considered the leader of physiocrats, said that in the state of nature the ordrenaturel is indeterminate. Physiocrats attached importance to the divine character of the ordrenaturel.

Mercier de la Riviera, a physiocrat says that "the social order is not the work of man but is, on the contrary, instituted by the author of all nature himself, as all the other branches of the physical order". They believed that men in society are subject to natural laws in the same way that equilibrium of nature is maintained by physical laws. These natural laws of society are

<sup>1</sup> Gaspard, Toufick. A Political Economy of Lebanon 1948–2002: The Limits of Laissez-faire. Boston: Brill, 2004.

<sup>2</sup> Journal Economique 1751, Article by the French minister of finance.

<sup>3</sup> M. d'Argenson, "Lettre au sujet de la dissertation sur le commerce du marquis de Belloni", Avril 1751, Journal Economique p.111



the conditions upon which depend wellbeing. As Dupont de Nemours put it: in general, natural laws are the conditions essential, according to which all the phenomenon of the world occurs. In particular, that part of the natural law which is relative to man comprises the conditions essential to the assurance of all the advantages which the natural order can afford. These conditions determine the use which we ought to make of our faculties in order to be able to satisfy our needs to enjoy to the fullest extent our natural rights. Physiocrats were influenced by the contemporary developments in the natural sciences and by the philosophy of Locke, Descartes, and Malebranche.

Following Locke, the Physiocrats emphasized the individual and “individual rights”. Private property was justified on Locke’s grounds: it is the expression of individuality, to which it is essential. Moreover, they believed that the individual should have a large measure of freedom in disposing of his property. But it must not be thought that they advocated an unlimited individualism, for that the rights of each limited the rights of the other, was clearly seen. The freedom of the foolish man must be restricted by the state in some instances. Mercier de La Riviere says, “The institution of private property and of liberty would secure perfect order without the help of any other law”<sup>3</sup>

“The laws of the natural order don’t in any way restrain the liberty of mankind, for the great advantage which they possess is that they make for greater liberty”<sup>4</sup>. “To secure the greatest amount of pleasure with the least possible outlay should be the aim of all economic effort. (Quesnay Dialogues sur les Artisan). And this was what the “order” aimed at.

The most influential writers among the physiocrats believed that individual knows his interest best or, in another word the individuals tend to act more in accordance with the law of nature than the government. It is of the very essence of that order that the particular interest of the individual can never be separated from the common interest of all, but this happens only under a free system. The basis of their whole economic system may be truly said to lie in the principle of “self-interest”. They assumed that the individual calculates advantage and disadvantages and recognizes the necessity of cooperating with his fellows, - on these assumptions they based their theory of society. Hence their well-known maxim, “Laissez-faire, Laissez-Passer”. That is, let things alone, let them take their course.

“The movement of society are spontaneous and not artificial, and the desire for joy which manifests itself in all its activities unwittingly drives it towards the realization of the ideal type of state” (Mercier de la Riviere). This is laissez-faire pure and simple.

Laissez-Faire does not necessarily mean that nothing is to be done. It is not a doctrine of passivity or fatalism. There will be ample scope for individual effort for it simply means leaving an open field and securing fair play for everyone free from at least fear lest his own interest should injure other peoples or in any way prejudice those of the state. It is true that there will not be much work for the government, but the task of that body will by no means be a light one, especially if it intends carrying out the physiocrats program. The only function of the government according to this doctrine is to protect life, liberty, and property. Since liberty and property spring from the very nature of man and are necessary to his individualism, human laws should merely recognize, formulate and maintain them.

<sup>3</sup> Mercier de la Riviere, l’ordre naturel volume ii, p.617

<sup>4</sup> Quesnay, Droit Naturel, p55



### **Functions of the state:**

Since the Physiocrats were ardent advocates of the principle of laissez-faire recognizing it to be the sine qua non of the natural order, they could very well be expected to oppose all legislation and authority. On the contrary, we find that they assigned important functions to the state. Simultaneous to their inaction in the self-imposition of the natural order upon all those who understood its superiority, they held that all people were not equally intelligent and even intelligent people needed education for understanding and obeying the laws of nature. It was chiefly with this end in view that they recognized the importance of the state. It can be very well inferred from their writing that they wished to reduce legislation to the barest minimum - abolition of useless laws and promulgation of laws which were essential for the preservation of the natural order.

As Boudreau wrote, “remove all useless, unjust contradictory and absurd laws and there will not be much legislative machinery left after that. These laws were simply to be the copies of laws of nature as Mercer de La Riviera held that “the positive laws that are already in existence are merely expressions of such natural rights”. In this context, it can be very well concluded that they wanted every law to be an expression or replica of that divine wisdom which rules the universe. And therefore, the state was to be the lawgiver and not the lawmaker<sup>5</sup>. They thus wanted to see the maximum of authority with the minimum of legislative activity. Their Ideal was neither democratic self-government nor a parliamentary regime. Both were despotic. Similarly, Dr. François Quesnay was of the opinion that government should be centralized in a single person, who, however, should be guided by the laws of nature. The chief of the state should be a protective sovereign and not a tyrant. Physiocrats believed that the government run by many persons leads to discord and commotion. The best form of government which they advocated was a single authority, vested with sovereign powers, but acting in conformity with the laws of nature and deriving the positive laws from these natural laws. They, therefore, desired to have a sovereign authority in the guise of a hereditary monarchy. In short, they wanted a benevolent despot. The chief function of the sovereign was to do all that was necessary for the preservation of the natural order and to defend private property against the attacks of the ignorant and sacrilegious. No order of any kind is possible in society unless the right of possession is guaranteed to the members of that society by the force of a sovereign authority.

Instruction is the second duty upon which the physiocrats lay special stress. “Universal education”, says Boudreau, “is the first and only social tie”. Quesnay is especially anxious for instruction on the “natural order” and the means of becoming acquainted with it. Further, the only guarantee against personal despotism lies in well-diffused instruction and an educated public opinion. If public opinion, as Quesnay said, is to lead, it should be enlightened.

The construction and maintenance of public works by the state is the third important function.

To conclude, we can say that the concept of a laissez-faire as advocated by physiocrats sought to minimize the function of the state to a minimum. Since they believed that individuals guided by their self-interest could best secure their welfare as well as that of society. So any action directed to restrict individual actions or activities could reduce the welfare of the society as such. The concept of laissez-faire which in fact was very dear to



classical economists had its origin to the physiocrats school of thought which later proved to be a cherished ideology upon which rested the development of latter economic theories. Physiocrats are to be believed the predecessors of classical economists. Adam Smith, the father of modern economic science was deeply influenced by the physiocrats school of thought and in particular by Dr. Francois Quesnay. It was under Adam Smith that the policy of laissez-faire was actually refined and nurtured which dominated and remained an important concern for the centuries to come.

### **Contribution to the thought of Laissez-Faire**

#### ***Laissez Faire as Given By Adam Smith***

Adam Smith is being recognized as the father of modern economic science. He collected the scattered ideas and knitted them together and gave them a final shape. He was an institution in himself. His masterpiece “**The Wealth of Nations**” published in 1776 contains his main economic ideas.

Smith’s moral philosophy supplies a basic framework of his economic thinking and reasoning. His moral philosophy is a part of the development of eighteenth-century British thought that arose as a reaction to Hobbes “selfish system”<sup>6</sup>. In Hobbes philosophy “self-preservation” or what we call “selfishness” motivate every human action. Hobbes maintained that to let this selfishness guide the action of a man is quite dangerous. If this approach is adhered to, there would be a universal and disruptive state of war between man and man. While cooperation and infact no war were the real need. Hobbes implied that the only way to preserve or protect the society and save it from the clutches of war would be an effective intervention by the state –for which state may resort to the use of force if the need is felt. This approach underlying Hobbes philosophy paved the way for the subsequent development on the subject “state intervention” which eventually was taken up by Adam Smith and treated it explicitly and eloquently.

Lock attacked the basic idea of Hobbes reasoning. Lock maintained, what resulted in conflict between men and men is the “Niggardliness of nature”. Nature does not provide enough of resources needed by man and this causes a conflict between human beings. The conflict or war thus is not the result of selfishness or self-presentation and the “state of nature” is essentially good. The state would, therefore, step in to help the society in overcoming this scarcity which is the basic cause of all conflict. We find that both Hobbes and Lock’s ideas were implying “state intervention”. In Locke’s, state was meant to mitigate scarcity of resources while in Hobbes it was meant to preserve order. However, Lock admitted that state could not bring about a complete removal of scarcity and therefore inequalities of income and wealth were bound to be there and it was the duty of the state to preserve these rights and inequalities. Lock failed to see that the state could even act in a way which would spread “scarcity” evenly for everyone.

Hume’s reaction to Hobbes was on a different plane. To Hume “sentiment” was an important motivating force in guiding human actions. This “sentiment”, he termed as “benevolence”, “humanity” and “sympathy”. This way human actions were virtuous and beneficial both for the society and the individual. Hutcheson’s approach was also similar to Hume’s. He subscribed to that atmosphere of optimism which prevailed during that period. Science had

<sup>6</sup> Claudio napoleoni, op.cit, p25



progressed by great strides. Hutchison's belief thus rested upon the capacity of man to harness nature to his will. This dream was expected to solve the problem of scarcity forever. In the achievement of happiness, there would be no handicap or barrier like niggardliness of nature. An achievement of this state of affairs would extend lock's logic to the conclusion that to the event of there being no scarcity, there would be no conflict between men. Hutchison stressed both benevolence and utility as principles that would explain the harmony of interest in society. He believed that man was essentially benevolent (a sentiment that was echoed by Hume also). To men, it was a pleasure to be benevolent. This way, the social and individual interests coincided. To be virtuous, therefore, meant to be a utilitarian.

Adam Smith was greatly influenced by Hume and Hutchison. Their influence would be seen in Adam Smith's economic ideas. We find, therefore that Smith had an occasion to see the presence of an "invisible hand" a guiding force in his predecessor's philosophical systems. In Hobbes, it was leading to a perpetual conflict and had to be replaced by state intervention. In Hutcheson and Hume, it was providing benevolent guidance. Smith, however, modifies the basis and operation of the invisible hand. "To him, it is not the benevolence, altruism or anything like that which brings about a harmonious state of affairs. In Smith, everyone acts according to his self-interests but that it leads to the benefit of both the individual and the society. In this stand, Adam Smith owes a debt to Bernard de Mandeville's "Fable of the Bees" from which it was clear that egoism was not evil and altruism was not necessarily good. It was realized by Smith that "it is not from the benevolence of the butcher or the baker that we expect our dinner but from their regard to their own interest". He maintained that unless individuals are selfishly motivated, the very process of economic progress would come to an end. In a way, Smith was making use of Hume's principle of utility. In his system, every individual contributes to the overall social benefit by trying to maximize his own utility through exchange and production. Moreover, Smith introduced a further conceptual modification in his reasoning. While in Mandeville, the pursuit of self-interest was a vice", this was not so with Smith. To him, such a behavior was guided by some positive tendencies. In this connection Spiegel, while talking about Smith's ethics, says that "what sympathy accomplishes in the moral world, self-interest does in the economic one".<sup>7</sup>The hype of "invisible hand" Smith conceives does not create any conflict between social and individual ends.

Smith proceeded on the basis of certain hypotheses derived from the stand that human conduct was actuated by six motives namely: Self-love, sympathy, the desire to be free, a sense of propriety, a habit of labor and the propensity to truck, barter, and exchange one thing for another. From these spring boards, Smith was able to conclude following:

- 1) Everyone has a Scotchman in himself that is to say; everyone is bound to act on the basis of self-interest. This premise is incorporated in the classical and neo-classical economics by giving it the name of economic "rationality" to try to serve one's own interest is to act rationally. There is an invisible hand guiding the behavior of every individual economic unit.
- 2) Everyone wants to improve his condition. This implies that man is not only trying to safeguard his existing interest, he is keen to further them also, if possible.

<sup>7</sup> Henry William Spiegel, the growth of economic thought, prentice hall, 1971..p229  
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- 3) Everyone is the best judge of his own interests. The state or any other agency is not competent to judge that on behalf of others. Therefore, given freedom to act, everyone would be able to judge what he should do and would believe accordingly.
- 4) Smith believed that interest of different economic units did not conflict with one another- they went in harmony. The working of the invisible hand leads to the benefit of society. The different motives of human action were so carefully balanced that the benefit of one could not conflict with those with those of others, so long as the society was not riddled with artificial barriers, e.g. state regulation and monopolies. As a result, each individual was led by an invisible hand to promote an end which was no part of his intention.
- 5) Smith further maintained that there were certain instincts which led to new act and create a certain institution which was not only spontaneous but also necessarily beneficial to the society.

Smith's system, so long as it was not obstructed by the activities of the state, was sure to improve the economic conditions of the society steadily. Opulence was bound to grow. Smith's system, therefore, led him to insist on a kind of individualism in which individual instincts, self-interest, and decision making must be given free play. In smith, individual interests were bound to be compatible with social interests. But to ensure such a compatibility it was essential to ensure economic liberty as well. The restraints on individual actions were not those of the state which was always a worse judge of the interests of others, but by the forces of competition themselves with certain specific exception viz, "those exertion of the natural liberty of a few individuals which might endanger the security of the above society, are and ought to be restrained by the laws of all government"<sup>8</sup>. Smith, in the same way, recommends the coverage of sanitation, primary education, and state examination as a condition to entry into the liberal professions. The state, therefore, must adhere to the philosophy of "Laissez-faire" and only to a restricted sphere of economic activities, that is, the creation and maintenance of social overheads.

Smith, following the physiocrats, but in a more comprehensive and scientific fashion, finds himself driven to the same conclusion, namely, "the wisdom of non-intervention" by the state in the matters economic"<sup>9</sup>. He is not satisfied with proving the inefficiency of intervention as compared to the efficiency of those institutions which are spontaneously created by society itself, but he attempts to show that the state, by its very nature, is unfitted for economic functions. The governments are "always and without any exception, the greatest spendthrifts in the society. "The reasons for this are numerous:

In the first place, they employ money which has been gained by others and one is always more prodigal of the wealth of others than of one's own.

Lastly, the state is an inefficient administrator because its agents are negligent and thriftless, not being directly interested in administration, but paid out of public funds. Should the administration of the land pass into the hands of the state? He

<sup>8</sup> Adam smith, wealth of nations, op.cit.p308

<sup>9</sup>Ibid,bookiv,chapter9 in volume5;p104



exclaims that not a fourth of the present produce would ever be raised, because of “the negligent, expensive, and oppressive management of his factors and agents”<sup>10</sup>. On the contrary, he proposes that the remainder of the common land should be distributed among individuals. For the same reasons the necessity for stimulating personal interest wherever possible he commands, instead of a fixed salary for public officials, payment by those who benefit from their services, such payment in every case to be in strict proportion to the zeal and activity displayed. This was to apply for example to judges and professors.<sup>11</sup>

Non-intervention for Smith was a general principle and not an absolute rule. He was too doctrinaire, and he never forgot that to every rule there are some exceptions. An interesting list could be made, giving all the cases in which according to Smith, the legitimacy of state intervention was an indisputable legal limitation of interest; state administration of the post office, compulsory elementary education, and state examinations as a condition to entry into the liberal profession or to any post of confidence.

The whole of Smith’s work is a plea for the economic freedom of the individual. It is an eloquent appeal against the mercantilist policy and violent attack upon very economic system inspired by it. At this point, there is an absolute agreement between the work done by Smith in England and that carried on at the same time by the physiocrats in France. Now we can pronounce the functions of the state in more explicit manner. In passing to book v, “The revenue of the sovereign or common wealth”, Smith takes occasion to make a formal statement of the important duties of the sovereign according to the “System of natural liberty”. These duties or functions are as follows:

- i) the duty of protecting society from the violence and invasion of other independent societies;
  - ii) the duty of protecting, as far as possible, every member of society from the injustice or oppression of every other member of it or the duty of establishing an exact administration of justice; and
  - iii) the duty of erecting and maintaining certain public works and certain public institutions, which it can never be for the interest of any individual or small number of individuals, to erect and maintain,..... though it may frequently do much more than repay it to great society”<sup>12</sup>. The establishment and maintenance of certain public works and institutions are divided into:
    - a) The institutions and public works in favor of trade and commerce, as streets, canals harbors, embassies, fortification in countries belonging to barbarous people;
    - b) The education of the youth i.e. a school system;
- c) The education of the entire people i.e. the church

He holds that church and state should be independent of each other. The church, the school, streets, harbors, and similar public works are beneficial to the entire society, and it would

<sup>10</sup>ibid, book v, chap 2, part ii; vol ii, p308

<sup>11</sup> Ibid, book v, chap 1 , part iii, vol ii, p 250

<sup>12</sup> Ibid, book iv, chap 9, p 185



really be no injustice if society were required to defray the expense of their establishment and maintenance; but as they benefit especially those who use them immediately, it is to be recommended that such users pay for them.

These excerpts seem to make Smith's position clear enough. He admits several particular exceptions to the general principle of laissez-faire. Put in concrete terms, the exceptional cases in which the government might properly interfere, were:-

- a) In Foreign commerce: Taxes on imports were justifiable in order to make a nation self-sufficient in such things as saltpeter, and in shipping; and also, if goods produced at home were taxed, imports of these goods should bear a similar tax. If English products were taxed in foreign countries, it would then be "a matter of deliberation" whether foreign taxation could not be abolished by retaliatory duties. A duty on exports of wool was to be favored under certain circumstances.
- b) In banking where the liberty of few endangers the liberty of the whole society, it ought to be restrained by law.
- c) Interest Rates- Smith thought that the rate of interest should be legally fixed though with due regard to the market rate.
- d) Education in the case of those who could not afford an education, the government might profitably provide for free schooling.

### **Laissez-faire by Jeremy Bentham**

Laissez Faire as given by Jeremy Bentham, although not primarily an economist, influenced the development of economic thought so considerably, and in such an interesting way, that even a brief history of the science must discuss his contributions. Between the years 1787 and 1798, he published that part of his work which is most significant to the economist, thus following Adam Smith by about a decade and Preceding Ricardo. He was essentially a social philosopher and was more interested in government and law than in economics.

Bentham maintained that compatibility between individual and social interests was essential if the "The Greatest good of greatest number" was to be guaranteed. In Adam Smith, such a compatibility of interests was ensured by the guidance provided by the "invisible hand" of self-interest. In Bentham, on the other hand, the individual action was to be guided by the dictates of pain and pleasure. Bentham was, therefore, to show that such actions on the part of the individuals were compatible with the general interest of the society. The pursuit of maximum happiness on the part of every individual was to lead to the greatest good of the greatest number. To this end, Bentham conceived the restructuring of the government, the legal system, and the society in such a way as to ensure this compatibility of individual and social interests. Bentham attributed the gap between the ideal and the actual behavior of individuals to two things:

- 1) The first thing was the deficiencies of man's knowledge and reasoning. These deficiencies should be removed through improved and universal education so that the individuals are enlightened as to their true interests. This education itself will include the "conditioning" of human behavior and reflexes through forming the minds association-patterns. These association patterns are to be evolved through a reward



and punishment method whereby any action which causes harm to others attracts a penalty greater than the benefit to the doer. Such a form of education was, in reality, more elaborated and advocated by James Mill.

- 2) The second step was to reform the government and legal system of the society. The society, to Bentham, is composed of individuals and its aggregate happiness can be taken as the equivalent of the summation of individual happiness. Accordingly, it is imperative that any possible conflict between individual interests be removed. As it was, individual actions might be contradicting each other's interests and that of the society on account of ill-organized government and the legal system. He assumed that given the requisite education, every individual would be a better judge of his own interests. This, therefore, pointed towards a particular rate for the government.

On the one hand, it was to follow a laissez-faire policy and the other it was to reform the legal system appropriately so as to ensure that none inflicted more harm than he gained by any action of his. An aristocratic state could not be expected to formulate laws which would satisfy the above-mentioned rule. "If a government is to be expected to remake all law into what it should be, i.e., to make and administer all and only the laws required to advance the happiness of the people generally, then this must be a government so framed as to fully align the self-interest of each legislature and official with the interest of desires of the people or of the majority of them. And this means that it must be a political democracy, in which only the governors who best serve the governed can both gain and retain powers"<sup>13</sup>.

It may be emphasized that Bentham's laissez-faire is different from Adam Smith's. Adam Smith's Laissez-Faire followed from his "Naturalism" based upon spontaneous actions of the individuals and the resultant spontaneous and beneficial institutions. To Bentham, on the other hand, the conclusion of Laissez Faire comes as a result of deliberate choice, as a result of the intellectual decision and rational thinking. There was no metaphysical assumption involved in Bentham as was the case with Adam Smith. Bentham's system was based upon rational tests. Furthermore, Smithian system was running in terms of economies only and need not be associated with or dependent upon the other aspects of the social organization. But Bentham's system was more comprehensive and involved the whole social system. His Laissez Faire was conditioned by the democratic form of the government and the necessary education of the masses. Also, Smith's system only touches the fringe of Hedonism or the utility fields. Bentham plunges right into it and bases all his reasoning in terms of this utilitarianism.

#### **Government interference: Laissez-Faire by John Stuart Mill.**

John Stuart Mill is sometimes referred to as the last classical economist. It is claimed that he stated the classical position in its final and most systematic form. Mill's contention that production is subject to immutable laws of nature, while distribution is subject to the laws of human institutions, led him to recognize certain areas of government intervention and formulate his socialist program. Government interference, according to Mill, should be limited by a general right of citizens to their individuality, in so far as such a right is not injurious to others, -if I do not injure my fellows, I may be or think as I choose "all restraint,

<sup>13</sup> Overton H. Taylor, op.cit., p124



qua restraint, is an evil”<sup>14</sup> and a point greatly emphasized, is that a large degree of individual initiative is desirable as a means of education.

He also considers that division of labor may be unduly restricted by the inability of the government to do all things, there being limitations upon its activity which do not obtain in the case of its individual members. This limitation might be more or less overcome by greater division in administrative function; but on the whole, Mill thinks that private activity is generally better and cheaper, as is shown by the fact that the government is seldom able to compete with private individuals. Like his classical predecessors, Mill held that the individual has both greater knowledge of his own feelings and circumstances and more interest in his own well-being than anyone else; accordingly, individual initiative is desirable except when it harms other individuals or impedes their efforts to obtain their own good.

In his essay in liberty”, Mill also portrays vividly the dangers of bureaucracy, showing how it substitutes routine for progressiveness and being insufficiently subject to criticism, rushes into ill-advised crudities of policy.<sup>15</sup>“Laissez Faire, in short, should be the general practice; every departure from it, unless required by some great good, is a certain evil”. But Mill allows a great place for government activity. The utility is the only test: if the greatest good of the greatest number is thereby conserved, let the government step in. He distinguishes two great classes of interference, according to the method; “Authoritative” in which the government says, “do this” or “do not do that”, “Non-authoritative”, or optional, as when the government merely spreads information, establishes models and the like. The burden of proof rests heavily upon those who advocate the former; the latter is less open to objection.

More specifically, Mill would permit government action in assets in which it is required by the interests of consumers who are unable to help themselves. Here the competition of the market does not apply. The matter of schools, for instance, cannot be left to the judgment of individuals. In the interest of the incompetent as the insane; of those under a personal contract in perpetuity, as married women; and of those who have but an indirect control over their property, as investors in joint stock companies, governments may properly interfere. Similarly, where people are acting for others and are not properly guided by self-interest as in the administration of the charity, and in such public service as erecting lighthouses or conducting scientific experiments, there is room for public activity. Mill was not committed to individualism as an absolute generalization. The influence of Bentham’s thought is thus apparent.

#### **Government intervention- as given by Fredric Bastiat.**

As everything in the field of value and distribution tends to work out harmoniously, if left alone, Bastiat considered that the science of government is exceedingly simple. Government. performs its functions by the exercise of force, and there is only one place where it has, in his opinion, a moral right to exercise of force, that is in establishing justice. The action of government is “essentially limited to the maintenance of order, security, and justice. All action of government beyond this limit is a usurpation upon conscience, upon intelligence, upon industry; in a word upon human liberty”<sup>16</sup>. This, of course, begs the

<sup>14</sup> Principles, Bk.v, chap 9

<sup>15</sup> On liberty, chap 3

<sup>16</sup> Harmonies Economiques,p4



question as to the justice of present arrangements and assumes the state of natural harmony of which he conceived, to exist in fact.

### **Critical evaluation of Laissez-faire**

The nineteenth century opened with a feeling of contempt for the government of every kind, and the unbounded confidence on the part of at least every publicist in the virtue of economic liberty and individual initiative. It closed amid the clamor for state intervention in all matters affecting the economic or social organization. In every country, the number of public men and of economists who favor an extension of the economic function of government is continually growing and today such men are certainly in the majority. To some writers, this change of opinion has seemed sufficiently important to warrant special treatment as a new doctrine variously known as “state socialism” or “the socialism of the chair” in Germany.

The doctrine of absolute laissez-faire was not long allowed to go unchallenged. From the time of Smith onward, there is an uninterrupted sequence of writers -all of them by no means socialist -who ventured to attack the fundamental propositions of the great Scotsman and who attempted to show that his practical conclusions were not always borne out by the facts.

Smith based his advocacy of laissez-faire upon the supposed identification of public and private interests. He showed how competition reduced prices to the level of cost of production, how supply adapted itself to meet demand in a perfectly automatic fashion, and how capital in an equally natural way flowed into the most remunerative occupations. This principle of identity of interests was, however, rudely shaken by the teachings of Malthus and Ricardo, although both of them remained a strong adherent of the doctrine of individual liberty.

Sismondi, who was the next to intervene, laid stress upon the evils of competition and showed how social inequality necessitated the submission of the weak to the will of the strong. His whole book was simply a refutation of Smith’s providential optimism.

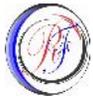
Stuart Mill, in the famous fifth book of the “principle”, refuses even to discuss the doctrine of the identity of interests, believing it to be quite untenable. On the question of non-intervention, he admits the validity of one economic argument only, namely, the superiority of self-interest as an economic motive. But he is quick to recognize its shortcomings and the exceptions to its universal operation in the natural incapacity of children and of the weak-minded, the ignorance of consumers, the difficulty of achieving it, even when clearly perceived without the help of society as a whole, as in the case of the factory Acts. In matters of that kind Stuart Mill was inclined to favor state intervention.<sup>17</sup>

M. Chevalier, from his professorial chair in the college de France, extended his congratulation to Mill upon his successful restoration of the legitimate duties of government.<sup>18</sup> Chevalier thought that those who believed that the economic order could be setup simply by the aid of competition acting through personal interests were either illogical in their arguments or irrational in their aims. The government was simply the manager of the national organization, and its duty was to intervene whenever the general interest was endangered. But the duties and privileges of government are not exactly those of the village policeman.<sup>19</sup>

<sup>17</sup> Liberty, chap 5,p228

<sup>18</sup> Michael Chevalier ,introductory lectures,no.10, vol I,p221

<sup>19</sup> Cours, vol I, p 211,214; vil ii,p 38,115



Every one of these authors in varying digresses, of course, admits the legitimacy of state intervention in matters economic. Liberty doubtless is still the fundamental principle. Sismondi was content with mere aspiration so greatly did the difficulties of intervention appear to him. Stuart mill thought theonus should probably rest with the innovator. Cournot considered liberty as being still the most natural and simple method, and should the state find it necessary to intervene it could only be in those instances in which science has clearly defined aim in view and demonstrated the efficacy of the methods proposed. Every one of them has abandoned liberty as a scientific principle.

Laissez-faire policy received a severe flow with the advent of the great depression of 1930's. This time it was John Maynard Keynes who dared to challenge the laissez-faireprogram. While Keynes retained certain classical doctrines, and did not attack classicism so much as he did certain contemporary economists (such as Pigou) supposed to represent it, his basic approach to economics is fundamentally different from that of classical economics. His thought is in line with the writings of many recognized opponents of the classical economics Lauderdale, Sismondi, Rae, Proudhon, Marx, and Hobson. Specifically, Keynes theory assumes that tendencies to save (to not consume) tend to become greater than tendencies to invest. He assumes that, in our advanced capitalistic economy, investment opportunity and the inducement to invest lag. But saving (not spending) goes on. Thus a gap arises between income and consumer spending which is too great for investment to fill. This reduces effective's demand, which tends to cause reduced output and employment. Finally, income and consumption are affected."<sup>20</sup> The amount of saving ("Surplus over consumption") is reduced, restoring the balance between saving and inducement to invest. But this partial and temporary "equilibrium" is one of less than full employment. It is not a desirable or very stable one. This makes the case for the government to step in. Thus Keynes came to the conclusion that private enterprise alone cannot be relied upon. And so we find that the progress of the thought since the days of the Adam Smith had led to important modifications of the old doctrines concerning the economic functions of the state.

## CONCLUSION

By the late seventieth century, an increasingly large number of capitalists, particularly those whose origins had been in the craft guilds, had come to be significantly inhibited in their quest for profit by the maze of mercantilist restrictions and regulations that had originally benefitted the great trading companies , they sought relief from these constraints. They also disliked the mercantilist remnants of the older Christian paternalism that had condemned greed, acquisitive behavior, and the desire to accumulate wealth. From the capitalists need to be free from the extensive economic restrictions grew the philosophy of individualism that provided the basis of classical liberalism? Many believed that in a competitive market that pitted buyer against the buyer, seller against seller and buyer against seller society would benefit most greatly if the price was left free to fluctuate and find its proper level. This belief that restrictions on production and trade within a nation were harmful to the interest of everyone concerned became increasingly widespread in the late 17<sup>th</sup> and early 18<sup>th</sup>centuries. At the same time, as the equally important change was taking place in the ways in which economic thinkers explained prices and the nature and origin of profits then came the

<sup>20</sup> General theory.p31,63,210



physiocrats. They believed that human society was pervaded by the principle of “natural order. They were the great advocates of laissez-faire i.e. they believed that the most useful work any legislative body can do is to abolish useless laws physiocrats believed that natural order is of perfect harmony every individual who knows the laws will take steps that will make him happy. They believed individuals tend to act more in accordance with the law of nature than God. Physiocrats believed that individual should have a large measure of freedom in disposing of his property. They didn’t advocate unlimited individualism, for they recognized that right of each limited the rights of the other their well-known maxim was laissez-faire, laissez-passer i.e. let things alone, let things take their course. So according to them the function of Government is to protect life, liberty, and property. They also emphasized on free trade within a country, and an impassionate appeal for the freedom of foreign trade. They also advocated freedom of labor. After this further improvement and the actual expositor of the concept, laissez-faire is Adam smith who expounded it explicitly and popularized it. For decades, this concept caught the imagination of economists, and for decades, this concept became the source of great discussions. To Adam smith, laissez-faire or capitalism, or as Smith calls it the obvious and simple system of natural liberty is asserted to be the best possible economic system. According to him, if the government did nothing either to encourage or to discourage the investment of capital in any particular sector, then the capitalist’s selfish quest for maximum profits would cause economic development to take place in accordance with this natural and socially beneficial order. Adam Smith concluded that government interventions, regulations, grant of a monopoly and special subsidies all tended to miss-direct capital and to diminish its contribution to economic welfare. Furthermore, such government actions tended to restrict markets and thereby to reduce the rate of capital accumulation, to decrease the extent of the division of labor and accordingly, to reduce the level of production.

Bentham was an ardent spokesman for a laissez-faire policy believing that the free market would allocate resources and commodities in the most socially beneficial manner possible. In his later writings, he fundamentally altered his position. It was a time when fingers were pointed at this concept (Laissez-Faire) and its demerit came to affront. In Bentham’s early writings, he accepted Smiths argument that a competitive free market would allocate productive resources to those industries in which they would be most productive. He, therefore, believed that government interference in the free market might very likely diminish the level of production. At best such interference could not possibly increase production. However by 1801 , Bentham’s opinion about government intervention in the economy had undergone a change he said saving might not be matched by new investment is this case saving would lead to decreased prices and production, profits would decline and so should investment in such a case Bentham argued, if the government increase the amount of money in circulation then the money introduced becomes a source of increasing wealth the second reason for government interference in the market was to lessen the socially harmful effects of great inequalities of wealth and income. Then came Karl Marx-the most vehement critic of Laissez-faire Policy .According to Marx, the capitalistic system presupposed a property-less working class and a wealthy capitalist class. As capitalism developed, wealth and power would become concentrated in the hands of fewer and fewer capitalists. So his analyses of



capitalism could have been the death of this policy but it survived till John Maynard Keynes came into the scene. At that time, there was a wide depression; Keynes gave the diagnosis of increasing government expenditure for correcting the imbalances. Keynes did not want to replace capitalism as Marx wanted. He just wanted to refine the capitalistic system so Laissez-Faire as adopted today is not that Laissez-Faire which was advocated by Adam Smith it has been replaced by a welfare program.

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