

# LIBERALISM, CAPITALISM AND INSTITUTIONAL DEVELOPMENT

## Jason Soon talks to Max Hartwell

**M**ax Hartwell was born in Australia but spent most of his distinguished academic career as an economic historian in Britain, where he now lives. From 1956 to 1977, he was a Reader in Recent Social and Economic History and Professorial Fellow at Nuffield College, Oxford. He made his most significant contributions to the study of economic history in that period. From 1957 to 1972, he was an Editor of the *Economic History Review*. He is, however, most famous for his engagement in the 'Standard of Living Debate' with noted historian Eric Hobsbawm where he challenged the notion, popularised by writers such as Charles Dickens, that the Industrial Revolution was a period of unmitigated misery for the working population in Britain.

Max was also a past president of the Mont Pelerin Society, which was founded by Friedrich Hayek to promote and discuss the ideas of classical liberalism and their application to contemporary society.

He spoke to Jason Soon on a recent visit to Australia.

**JS:** Though the differences may have been overemphasised it has been said that there are two views of economic development. One is that countries which have been successful in development have benefited from special ingredients often thought to be cultural in origin and institutional in form, and that these are not universal. The other is that development is inherent to all societies but positive constraints exist to prevent the translation of individual wants into societal behaviour, usually in the form of dysfunctional institutions. Where do you stand between these two interpretations?

**MH:** Looking generally at economic history, the two great problems were growth and dissimilarity. The most common explanation is resource-driven. But that doesn't explain why some countries with resources don't develop and others with poor resources do, like Switzerland, for example. So you must come back to your first explanation, namely that the level of development is very much determined by not only resources given but institutions which in the first place determine motivation and in the second place determine incentives.



An action is determined by particular individuals – entrepreneurs – who perhaps have an innate quality inherited, but to this is added education and just as important, values and motivations. Given this initial equipment they act according to their motivations and values and according to the opportunities their environment offers. The richness of this environment also depends on the preexisting stage of development but

to the extent that their actions are constrained – that's the second interpretation. Their actions are constrained by institutions, by social values, political forces, law and so on.

What's interesting is that some economies got it right. The big puzzle of modern economic history is why Britain led so dramatically and successfully in modern economic growth. Again, you do come back to looking very carefully at what sort of society it was, what were its resources and

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whether there were any particular events which at a particular time motivated or changed the institutional context in such a way that it allowed opportunities to be released.

I have no theory of economic history. I think that particular paths to growth are very much individual in individual countries. The only way you can talk sensibly about development is to talk about particular cases. On the other hand, I do realise that economic growth will be more successful if a society is rich in resources; if a society has the human capital; if there are a set of values which for various reasons favour growth like the so-called Protestant ethic and very importantly, a context of law which in particular protects actions through the 'rule of law' and is very vigilant about the rights of property.

JS: And this was true of England ...

MH: In the case of England, there's no doubt that from the middle ages on there were institutional factors, which included the law and government, which favoured growth more than it did in any other country. The particular legal-institutional set-up was adopted from around the seventeenth century to the degree that by the eighteenth century England was much more 'advanced' than other countries in the context, opportunities and the encouragement to growth which resulted in the Industrial Revolution.

In England there was a political system confined by the rule of law, there was a common law which was not a fixed body of law whereas in Roman law there was a fixed set of principles which you had to fit things into. In England the common law was really based on what were the best practices of the merchants, what happened in the past and so forth. It was flexible in a way that Roman law was not. Roman law had to be changed from the centre. Common law was changed in courts by judges listening to people arguing for their rights.

JS: In *Capitalism in Context*, you wrote that it was the nation-state which made possible the rationality of purpose which paved the way for industrialisation and modern economic progress. A lot of this had to do with the way

the nation-state was able to make the common law more efficient. So in fact a balancing act is required between capturing the respective virtues of common law versus legislation. For instance, Hayek was fairly nuanced about this. He thought that the common law was a generally superior way of producing rules because of its flexibility and openness to feedback but that there was a place in making corrections to evidently bad law through legislation; though he didn't suggest any procedure whereby the appropriate balance could be struck.

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MH: The history of English law reveals its superiority over the European law in the way it developed in its recognition of titles to property which were not real, for example, bills of exchange and mortgages. This recognition was reached in England around the eighteenth century and Lord Mansfield was largely responsible for this. That gives you some part of the explanation for England's early development.

The strength of local government in England was very important. By contrast, nearly all the continental European states were highly centralised. There were attempts in England by the Stuarts for example, to expand the central powers of the state but they weren't successful.

Another thing about legal institutions is that if you look at France before the Revolution you had these products of different types of law, different weights and measures and different currencies. England unified these things before other countries, so in that sense some national unity was important. By the sixteenth century, England had a uniform currency and no internal tariff barriers though it had some tolls that were charges for particular services.



The unity of the nation state was not a centralised unity but simply a recognition of a national economy through which goods could flow freely. One of my students wrote an article years ago about how interest rates varied throughout England. On the whole he found that there was some difference reflecting distances but that they didn't vary in any great way.

**JS:** But there is a tension between the need for some centralised way of making the common law more efficient and standardised where necessary while retaining its flexibility?

**MH:** Legislation was important in England. But it only became important in the nineteenth century. To a large extent this was commercially motivated. Paddy O'Brien demonstrated that the mercantile state legislated in favour of commerce and that partly explained why entrepreneurs were more or less free to do what they wanted. The mercantile state was, as Charles Wilson pointed out years ago in a very much neglected book, a preparation for what followed.

**JS:** To what extent do you think that debates about the uniqueness of the Industrial Revolution as a great discontinuity are relevant to the development of the East Asian economies?

**MH:** I think there's still a lot of work to be done on comparative economic development.

The only person doing very good work in this country on this issue is Eric Jones. In *Growth Recurring* he refers to China. China through the thirteenth century was more developed than Europe. But why didn't it go on from there? A very interesting question. I think government has a lot to do with it.

**JS:** Joseph Needham who wrote a lot on ancient Chinese economic history refers to the differences between the 'mandarin mentality' and the 'mercantile mentality'.

**MH:** Yes, they were rich in markets. China was a well organised economy. Grain flowed and goods flowed but

somehow the element of growth was lacking. The human capital was there. But again, values may have something to do with it. Weber wrote an essay comparing the Eastern countries with Europe. The Protestant ethic, was, he argued, unique among the great religions of the world in terms of its individualist ethic. The Eastern religions were more communitarian.

**JS:** But was it really so much a Protestant ethic? Entrepreneurship is especially vibrant among the Catholic communities in South America today for instance.

**MH:** Yes. There was a great book written years ago by H.M. Robinson which pointed out that Italy led in many ways. There was nothing particular in Roman Catholicism which would have denied entrepreneurship. It may well be because the existing types of states in some European Catholic countries didn't encourage entrepreneurship which led to the Protestant countries of Northern Europe leading in growth later.

One of the problems with comparative economic history is that you have to be massively learned to make any meaningful comparisons.

**JS:** Going back to European history, would you regard the growth of cities as very important?

**MH:** Yes, but then the growth of cities goes back to the Agricultural Revolution. If you have a subsistence economy, all efforts and resources go into getting enough to eat. Once you start to create a significant surplus you can afford to have a non-agricultural segment and then you get kings and

bureaucrats. The centre of cities is fed by the countryside. Then you have the creation of mini-states. In the same way, through the creation of surplus, you have the growth of cities after the Industrial Revolution. But it came first

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with the Agricultural Revolution. This and the Industrial Revolution led to a huge growth in population which we are still benefiting from or suffering from.

Incidentally, I noticed that Jeff Kennett has opened his mouth recently about the population issue. Actually, what he said was quite sensible but it was taken out of context. Of course Australia could do with a much larger population. But that's another issue ...

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**JS:** After the city-state came the nation-state and that takes us back to what you said before about the nation-state being the focus of growth and modernity. Do you think that comments about the impending death of the nation-state are much exaggerated?

**MH:** What we've seen in the last few years is the great effervescence of attempts to create new nation-states. You'd almost call it tribalism. I don't think the nation-states are going to disappear in any way. The worst of this is in places like Yugoslavia and East Timor.

How to control it? The great liberal society is the society which recognises conflict and develops institutions which contain the conflict without violence. That's the problem internationally now. How do you control the nationalism which has been encouraged by the UN?

I think that the nation-state is not necessarily the perfect geographical unit for growth. To a large extent nation-states developed through politics but language is one of the determinants. You think of the French state in terms of its linguistic grouping but then this isn't true of Switzerland.

**JS:** It's interesting that you mentioned Switzerland because this relates back to your point about developing institutions which accommodate potential conflicts. The

Swiss cultural groups seem to have done this fairly well with their highly decentralised federalism.

**MH:** Yes. I was influenced as a student by John Anderson, a philosopher, a fascinating man. He influenced me in two ways. He reinforced views I had on two issues. First of all, what you might call scepticism. There are no authorities, or an authority is only as good as his argument and his proof. That's very important. The second is interdependence, that all of what we do has repercussions and you can't understand any social event without looking at the interdependencies but also recognising the idea of harmony of interests. That brings me back to one of the main virtues of liberalism. It doesn't try to reconcile so much as it tries to think of institutions which prevent or divert potentially serious conflicts.

**JS:** You have an interest in the origins of personal political beliefs. Given what you have said, would you then attribute your liberalism to these philosophical stances reinforced by John Anderson?

**MH:** Well, it stems from being an Australian. I was brought up in the northern tablelands of NSW. I was unaware of the state when growing up. In the village there were no public servants. Well, there was a schoolteacher. We never saw a policeman, or only did so once in a blue moon. There was no substantial welfare state. There were widows' pensions and soliders' pensions. There was a great deal of mutual assistance. There was a very, very deeply held belief that what you did was your responsibility and if you wanted to get on with the world you had to work hard and no one was going to help you.

On the other hand, as I grew up, I saw that Australians also believed that government had a very important role. But I think this basic individualism grew out of my

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background and was then reinforced by my study of history. For example, from reading a book like T.S. Ashton's *Industrial Revolution*, which was to me a revelation when I was a young lad.

The other side of Australia, of course, was mateship and cooperation. You help your mate and your mate helps you, and also voluntary association. I think that is the sign of a good society.

**JS:** In fact, in your short memoir in *Capitalism in Context*, you equate mateship with voluntary association.

**MH:** Yes.

**JS:** It doesn't seem to be the view of, for instance, those on the Left, who have appropriated the term as one of egalitarianism.



**MH:** Well, as you know, perhaps the most interesting and puzzling problem of history is why two historians on the same evidence come to divergent views about what happened. I put it down to confusion of what you're talking about and political views.

**JS:** It's interesting, though, that you characterise Australian society as inherently individualistic while at the same time, Australians have a very complacent view of the state as a benefactor and dispenser of goods. On the other hand, the Americans who are seen as individualistic are said to have a suspicious view of the state.

**MH:** I think Australians are getting more suspicious of the state. Australian attitudes have been complacent but then again there are many views of the state. Anarchism, I think, is just nonsense. I go for the J.S. Mill view that the biggest, most important and abiding question is what are the proper limits and functions of the state.

I would go back to Adam Smith – law and order, defence and public goods. There are public goods. You can argue about the extent to which health or education can be a public good but I don't think there's any doubt about the need for, say, law and order.

**JS:** What are your views about the proper governmental role in the alleviation of poverty? There is a distinction between absolute and relative poverty but then again the poorest people today are better off than the wealthiest centuries ago in the absolute poverty sense so it may not be a useful distinction. Recent research also suggests that there are significant health and well-being effects from feelings of relative deprivation. To what extent should liberals revisit their views of poverty alleviation in light of these facts?

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**MH:** There are really two types of poverty. One says, 'I'm poor because you're rich.' But the second is socially defined poverty. We've reached the stage in Western society where some group of people get in and say that the lower one third of incomes are poor. If you do that you have to keep on changing the line.

I do think that the charitable sense of poverty or poverty as we saw in the nineteenth century has by and large ceased to exist in Western societies. But that doesn't mean that there are not underprivileged people in society. Take health. Health is in some sense an accident of birth. Some sort of social insurance policy is needed.

**JS:** In your writings you emphasise the significance of the British cultural heritage to Australian society and its individualism. Do you think that enough attention has been paid in recent historical writing to this?

**MH:** When I went to England, I was influenced by people saying that Australia was more like the US than England. But when I went to the US I found out how profoundly British Australia is. There's no doubt that the intellectual and cultural baggage of individualism and secularism that the convicts brought with them was vital

to the success of this country. I don't think it has been much emphasised.

**JS:** Do you think that the debate over the republic and Australia's place in the world will make much of a difference to the embeddedness of these institutions?

**MH:** It's not going to fundamentally change anything. I think the republic is inevitable. What is important is what they decide to do by rewriting the constitution and they could make a mess of it, which would be disastrous. I think that the impact of Asian societies and economies on the whole have been beneficial, gastronomically if nothing else. But I don't see our institutions being greatly affected.

A lot of nonsense has been said about multiculturalism. It's like feminism. You have citizens and you give them the same rights and opportunities and you shouldn't do much more unless there are good reasons. If you have racial abuse, then yes, you should have some legal restraints there. I really believe that opening up Australia's doors and bringing in Asians and Southern Europeans and so on have been more or less entirely beneficial. But of course there are strains.

I remember years ago when I was here doing some teaching of English to migrants. Back then we had to teach them to assimilate. I remember protesting this because they interpreted assimilation as getting rid of migrants' cultural differences. That's gone now but then it has gone in the opposite direction.

Of course Australia will change with the changing nature of its population. I believe it already has. As a visitor the most obvious change is in gastronomy.

Also, the cultural life of the big cities has been diversified and a very high percentage of the population live in cities.

Another thing that has changed is orientation. When I was at school we used to talk about the Far East. It was as though we were in the Atlantic somewhere. There was practically no mention of Japan. There was a feeling of being part of the British empire. People are now very much more aware of the geographical situation and isolation as a European community. The greater awareness came with

the war. The only people we could turn to were the Americans. The great powers of the Pacific then were Japan and the US. In the future it will almost certainly be China.

All this is beneficial. We should be realistic about where we are. We thought then that by being part of the Empire, that enhanced our importance, which it did. The idea that Australia was an exploited economy is nonsense.

**JS:** Indeed, you have written that Australia benefited from being a supplier of raw materials to Britain during the Industrial Revolution. When do you see the turning point in the change in Australia's role in the world economy as being and what will be its future sources of growth?

**MH:** In the past, Australia was one of the suppliers to the Industrial Revolution, as was the US. The enormous demand created by the industrialisation of Europe opened opportunities for the growth of raw materials. We were to a large extent agricultural and mineral. We changed, but not dramatically. Until

World War Two, our main export was still wool. The formation of the European common market has reduced our role in Europe. That coincided with the growth of the Asian economies. Japan then became a great purchaser of our wool and coal. It's not as though our markets disappeared.

We are now an industrial economy. I think that Australia will go on growing its industrial base and become more refined and specialised. I don't think that Australia's role will change significantly. However, the second most important wine supplier to UK and France is now Australia. That's a success story of the last thirty to forty years.

**JS:** As a past president of the Mont Pelerin Society you came to know Hayek. One of the most remarkable things about Hayek was the multifaceted nature of his work. He wrote books on technical economics, intellectual history, jurisprudence, economic history, political philosophy and theoretical psychology. This is a quality which is rare today, especially among economists. Do you see this as a fair comment and if so how can we remedy the situation?

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### There's no Western country that's not suffering from the welfare state.

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**MH:** Well, I don't think you can do anything. The profession will do it gradually when they realise that they are not getting the answers. In my time when I did economics in the 1930s, you didn't have to know any math. I actually had done math in uni but everything in economics was explained in sentences. Now some of the few economists who do this who are also Nobel laureates are Coase and Buchanan. Coase wrote two articles, both of which are understandable, written without any equations.

The problem you mentioned will solve itself. You can't pass a law. You can only do it by people like Hayek, Buchanan and Coase producing such good economics which explains real activities. The case of Hayek is interesting because he got his Nobel prize for economics but of course his main work has been in social philosophy.

**JS:** What do you most get out of Hayek's work?

**MH:** I think that he didn't give me a great deal more than I had before, but I just admired a man who could do so much and do it so well. I think *The Constitution of Liberty* was my favourite book. I think that's a remarkable book. There was enough in the footnotes to last you a century. But again the phrase that sticks in my mind about Hayek is the 'unintended consequences of good intentioned actions' and that is now such an obvious point, but important.

There are three basic beliefs in the 1940s and '50s that are not accepted today. The first is that trade unions are only interested in furthering the interests of their members. Baloney. Increases in wages can have adverse effects on economic growth and inflation. In any case they harm the interests of the unemployed. The second one is that public servants are only interested in the public. Baloney. Public servants are just like everyone else. The third one is the idea of planning, the fatal conceit, that governments can define an objective and then define the means of getting it by the manipulation of a few key variables. We all know that's nonsense today.

**JS:** Does Hayek's analysis in *The Road To Serfdom* have any application today? I am thinking in particular of the

contrast between what you perceived as the robust individualism of your childhood and conditions today.

**MH:** There's no Western country that's not suffering from the welfare state. The old idea of the welfare state as I understand it was that you could identify in society people who were worse off like widows and you helped them. In other words, welfare was targeted. Since then it's developed into compulsory consumption. We say that you must take what's given by the state and it's absurd. The means test is difficult but then again why should people, for example, not pay to go to the Art Gallery where there are some of the great artifacts of mankind when they are willing to pay \$8 or more to go to see a movie or the football?

But then all Western societies run into budgeting constraints because what people don't like is increased taxes. But no one wants to lose the advantages they have in terms of welfare. So I don't think that Australia is any different from anywhere else. It will get worse, before it gets better, I suspect. One pressing issue is the changing age structure of Australia and its implications for our subsidised health system.

**JS:** That brings us back to what you said before about Jeff Kennett's contribution to the population debate.

**MH:** You could probably have 100 million people in this country. I've no idea how you'd measure the carrying capacity of Australia. But it's obviously much greater than

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it is today. I don't know anyone these days who would have more than two children. I think each generation gets an idea of an ideal sized family. It's partly determined by the cost of bringing up children and other factors.

We are at a very interesting stage in Australian history. The only group in this country I'm worried about is the Aborigines. It's quite clear to me that all Aboriginal policies have been a resounding failure. I was in Alice Springs recently and it was shocking to see their condition. It was an affront to civilised society. I don't think it's beyond the wit of a rich country like ours to do something.

**JS:** Do you have any thoughts about what can be done? What can be done besides specially targeted policies?

**MH:** You can't do it quickly but you've got to get them off welfare dependency. Education is the main thing. What you need is more Aboriginal teachers, nurses and doctors. And you don't do this by taking the children and trying to bring them up. That's nonsense ... that's not just nonsense, it's evil. I haven't got any solutions. It's not Aboriginal land rights. Though that's part of the process, it's not going to solve the problem.

**JS:** More than a decade ago, you wrote a post-mortem for the anti-capitalist mentality. Would you revise your opinion today?

**MH:** You might say now that everyone believes in the market. It's not anti-capitalism so much but the widespread view that the market doesn't do everything that's desirable in a good society. Well, I can go along with that. The old fallacy that you can slug the rich to improve the poor tremendously – if you took all the wealth away from the very wealthy, that would make very little difference to those on below average incomes. The desirable thing to do is to keep on plugging away about the efficiency of the market in allocating resources and the undesirability of Leviathan.

**JS:** I suppose it's a problem that intellectually, people can accept the benefits of free trade, for instance, but then they suffer the effects of uncertainty introduced by free trade.

**MH:** We also suffered from the uncertainty introduced by the invention of the railways and the cotton machine. It's the failure of the market which is the issue, again and again. If you take, say, Blair, he isn't anti-market. In fact,

he goes out of his way to favour the market. I remember a colleague of mine, Bede Nairn, he wrote a book called *Civilising Capitalism*. That's what the issue is these days. It's no longer the anti-capitalist mentality which is focussed on particular individuals, it's the anti-market mentality and I think that's more desirable. It's an improvement on debate before.

I remember when I was lecturing at Oxford, a student stood up and said, 'Everytime I see a Rolls Royce I feel lessened in its presence.' I said, 'I feel reassured – it's a sign of high tech ingenuity, good craftsmanship, hard work and beauty.' And he couldn't see that at all. *Policy*

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