Finance and Ethics in the History of Political Economy

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Prepared for the
Canadian Political Science Association
Annual Conference

Toronto, Ontario
June 1–3, 2006

Abstract

International financial structures and practices are widely recognised as having a profound impact on individuals' life opportunities. They are thus important objects of normative political inquiry. Still, the contemporary literature in international political theory has little to say about financial globalisation. At same time, normative reflections in the literature on the political economy of global finance remain underdeveloped. In short, the two literatures are broadly marked by a case of mutual neglect.

This paper begins the project of rectifying this mutual neglect by recovering insights from the history of political economy. I recover a tradition of thought that I refer to as "normative monetary thought." I trace the development of normative monetary thought through Aristotle, St. Thomas Aquinas, David Hume, Adam Smith, Jeremy Bentham and John Maynard Keynes, demonstrating how each considered the ethics of then-extant financial structures and practices.

Résumé

Les structures et pratiques financières internationales ont des effets profonds sur les circonstances de vie individuelles. Elles sont ainsi les objets importants pour des enquêtes normatives, mais la littérature actuelle sur la théorie politique internationale a néanmoins peu à dire au sujet de la mondialisation financière. En même temps, les réflexions normatives dans la littérature sur l'économie politique de la finance mondiale restent sous-développées. En bref, il existe un cas de négligence mutuelle entre les deux champs de recherche.

Cette étude commence le projet de rectifier cette négligence mutuelle en récupérant certaines idées dans l'histoire de l'économie politique. Je récupère une tradition de pensée que j'appelle la «pensée monétaire normative». Je suis le développement de la pensée monétaire normative par Aristote, Saint-Thomas d'Aquin, David Hume, Adam Smith, Jeremy Bentham et John Maynard Keynes en démontrant comment chacun a considéré l'éthique des structures et des pratiques financières de leur propre époque.

Introduction

> [B]etween the four basic social values of wealth, security, justice, and freedom, we have to ask both *how much* of each the [financial] system produces and *for whom* – security for whom, wealth for whom, justice for whom, and the freedom to choose for whom (Strange 1994).

> A study of the history of opinion is a necessary preliminary to the emancipation of the mind. I do not know what makes a man more conservative – to know nothing but the present, or nothing but the past (Keynes 1925: IX, 305).

There is growing recognition within international political economy (and political economy more broadly) of the ethical dimension of money and finance. Observers have noted that "ethical" investments constitute a sizeable and growing market segment in North American and European retail investment markets (Santiso 2005). As well, recent accounting scandals at Enron, WorldCom and Nortel have highlighted the place of ethical considerations in financial reporting (Straubus 2005). Perhaps most importantly, it is well documented that the structural adjustment policies prescribed by the International Monetary Fund have in many instances detracted from human welfare and the enjoyment of basic human rights (Aslanbeigui and Summerfield 2000; Franklin 1997; Thomas 1998).

These examples demonstrate that questions of ethics and questions concerning money and finance are often inextricably linked. Moreover, financial structures (particularly *global* financial structures) can – and often *do* – have a profound impact on individuals' life opportunities. They are thus important objects of normative political inquiry.[1]

Global finance, however, has not, to date, been made the subject of extensive normative political analysis. To be sure, there has been increasing criticism of international financial institutions such as the International Monetary Fund and the World Bank from elements of global civil society, and the criticisms levelled by particular activists are often ethically charged (Scholte and Schnabel 2002). Still, there exists little conversation between the scholarly literatures on global finance and global justice.[2] Indicative of this state of affairs is the comment of Devetak and Higgott that the question of justice "is underdeveloped as a subject of study under conditions of globalisation." At the same time, "the study of globalisation" – and one might include the literature on financial globalisation here – "has been equally blind to 'justice' questions" (Devetak and Higgott 1999: 484). Thus, the literature on the political

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1. Charles Beitz argues along similar lines in the 1999 afterword to his *Political Theory and International Relations* (1979). Beitz argues that "[t]he growth of the world economy since this book was written and the elaboration of global financial and regulatory regimes only strengthen the impression of an evolving global basic structure with consequences for individual life prospects..." (1999: 202). He later adds that "[t]his world contains institutions and practices at various levels of political organisation – national, transnational, regional and global – which apply to people largely without their consent and which have the capacity to influence fundamentally the courses of their lives." Given these developments, "principles of international justice are therefore of great practical interest" (1999: 204–205).

   In more abstract terms, John Rawls has argued that the choice of economic arrangements necessarily "involves some view of human good and of the design of institutions to realise it. This choice must, therefore, be made on moral and political as well as on economic grounds" (Rawls 1971: 259–260).

2. This is not to suggest that normative reflections on global finance are wholly absent from the literature on the political economy of global finance. One can point to recent work on legitimacy and accountability within global finance by Randall Germain (2004, 2001), Louis Pauly (1997), Tony Porter (2001), Sanjay Reddy (2003) and Ngaire Woods (2001). This work may be reflective of "a new preoccupation in the world of international finance – a desire to engage the ethical implications of globalisation" (Best 2003: 579). Such normative engagements with global finance, however, remain (often self-consciously) preliminary insofar as they do not make full use of the concepts and tools of modern and contemporary political theory. We therefore remain well short of a theory of *justice* for global finance. My doctoral thesis (in progress), entitled "Global Finance and Global Justice: An Integrative Theory" develops such a theory.

economy of global finance and the literature on global justice are marked, as Susan Strange (1970) might have said, by a "case of mutual neglect" not unlike that which existed between international economics and international relations in the early 1970s.[3]

The aim of this paper is to outline the history of ethical inquiry on monetary and financial structures and practices – a tradition that I refer to as "normative monetary thought" – and to demonstrate its utility to the larger project of theorising about justice in the contemporary context of financial globalisation. The major finding that this exploration of the history of political economy yields is that the present forced separation of finance and justice is the historical exception from the standpoint of intellectual history. Indeed, it is symptomatic of the "fifty years' rift" between international relations and intellectual history (Armitage 2004). Indeed, a survey of the history of political economy demonstrates that many questions about the ethical character of particular financial structures and practices have, in fact, been raised before. "A study of the history of opinion", to borrow an apt phrase from John Maynard Keynes (1925: IX, 305), thus recovers these forgotten insights. It also reveals theoretical continuities and episodes of conceptual change (cf. Schmidt 1998: 38). This paper therefore serves as "a necessary preliminary" (Keynes 1925: IX, 305) to my larger project of constructing an integrative theory of global finance and global justice.

The tradition of normative monetary thought, which can be traced from Aristotle to Keynes, stands in sharp contrast to the *positive* monetary thought that is the central concern of contemporary monetary economics and political economy scholarship on money and finance. Both traditions obviously subsume a range of divergent theoretical perspectives. Approaches to positive monetary thought do,

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3. Strange herself never framed the assertion in this manner – invoking her famous "mutual neglect" argument – though some of her last published writings make clear that she perceived a need to give serious consideration to the *normative* implications of globalised finance. In doing so, she advanced an implicit critique of the field of international political economy for having neglected this aspect of the topic (Strange 1998a, 1998b, 2002a, 2002b).

however, converge on an understanding of the *goal* of research on money and finance. The tradition of positive monetary thought prompts us to ask, for example, how internationally mobile capital *does* (or *does not*) impose constraints on governmental policy-making, how credit *is* created in the global political economy, and how financial orders *are* made and unmade. These are positive questions. The tradition of normative monetary thought rather prompts us to ask what *fairness* requires in terms of the distribution of benefits and burdens arising from particular financial practices, or what a *just distribution* of credit globally would be.

Aristotle

While the tradition of positive monetary thought is admittedly the more familiar of the two, the tradition of normative monetary thought has an equally impressive lineage.[4] The roots of normative monetary thought, at least in the West,[5] are in Aristotle's writings, whose influence can be seen in the writings of the medieval schoolmen on money, as well as in the writings of Adam Smith.[6] In approaching Aristotle, it is important to observe at the outset that contemporary distinctions between ethics, politics and economics find no analogues in the thought system of the ancient Greeks: "the Greeks did not develop economics as an autonomous discipline

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4. It is difficult to date the eclipse of normative monetary thought by positive monetary thought, as the intellectual history is untidy. The normative and positive elements of the monetary thought of Aristotle and the medievals prove difficult to delineate. Beginning with Smith, but made more pronounced in Ricardo and Mill, the classical political economists drew a distinction between the normative and positive elements of monetary analysis. With the increasing formalisation of *economics* (no longer *political economy*) brought about with the marginalist revolution and the rise of Marshallian economics, the study of money became strictly a positive science, not a moral one. Keynes – Marshall's student, no less – stands out as the notable exception from the twentieth century to this trend.

5. There is an equally rich tradition tradition of Islamic normative monetary thought which is not discussed here. On this, see, e.g., Choudhury (1997); Presley and Sessions (1994); Useem (2002).

6. Keynes, who continued the tradition of normative monetary thought in the twentieth century, and is discussed below, was rather influenced by particular strands of liberal economic and political theory than Hellenic or medieval writings.

but instead considered economic matters as part of their general inquiry into ethics and politics, and more important, their much wider study of the best social organisation of the city-state" (Petrochilos 2002: 600). For Aristotle, then, ethics and economics was subordinate to politics – the "master science" – which had as its aim the good of the community (Petrochilos 2002: 610).

Aristotle's discussion of money is found primarily in the *Politics* (I. viii–I. xi) where his aim is to delineate between those forms of wealth acquisition that are in accordance with nature (and are therefore morally acceptable) and those that are unnatural (and are therefore subject to disapprobation).[7] To understand how Aristotle reaches his conclusions about natural and unnatural forms of acquiring wealth, however, one must first consider his understanding of justice, nature and the relationship between the two.

Aristotle's discussion of justice in the *Nicomachean Ethics* describes justice as a mean, "because it is about an intermediate condition, whereas injustice is about the extremes." Injustice, for Aristotle, is "disproportionate excess and deficiency in what is beneficial or harmful". Just action, then, "is intermediate between doing injustice and suffering injustice, since doing injustice is having too much and suffering injustice is having too little." Conversely, unjust action means keeping for oneself "an excess of what is beneficial … and a deficiency of what is harmful…" (Aristotle 1999: 76).

There are clear parallels between the understanding of justice presented in the *Nicomachean Ethics* as an intermediate position between "excess and deficiency" and the understanding of nature as bounded, and what is "natural" as within limits, that Aristotle presents in the *Politics*. Aristotle connects his thoughts on justice and nature in arguing that the acquisition of territory through war is in accordance with nature, as there are "such men as are by nature intended to be ruled over but refuse." According to Aristotle, it is this "kind of warfare which is by nature just" (Aristotle

7. For a more detailed account of Aristotle's monetary thought, see Meikle (1994, 1995, 1996); Petrochilos (2002).

1981: 79). Although this passage will have objectionable connotations of both national chauvinism and imperialism for modern readers, our present concern requires us only to observe that, for Aristotle, what is just that which is in accordance with nature.

Aristotle further points to farming, piracy, fishing and hunting as "the main ways of living by natural productive labour". In channelling their labours into these pursuits, humans "simply live the life that their needs compel them to": the acquisition of goods through these means "is clearly given by nature herself to all her creatures" (Aristotle 1981: 78). Acquiring wealth by such means is, for Aristotle, "in accordance with nature, a part of household-management, in that either the goods must be there to start with, or this technique of property-getting must see that they are provided..." (Aristotle 1981: 79). Aristotle continues in arguing that "wealth in the true sense consists of property such as this" since

> the amount of property of this kind which would give self-sufficiency for a good life is not limitless, although Solon in one of his poems said, 'No bound is set on riches for men'. But there *is* a limit, as in the other skills; for none of them have any tools which are unlimited in size or number, and wealth is a collection of tools for use in the administration of a household or a state (Aristotle 1981: 79).

In discussing money specifically, Aristotle's writings centre on the concept of *χρηματιστική*, or *chrēmatistikē* (roughly translated as "wealth acquisition" or "money-making") and the distinction between natural and unnatural forms of *chrēmatistikē*. For Aristotle, the acquisition of wealth from the environment (e.g., by means of agriculture, fishing and hunting), barter, and the exchange of goods for money are "in accordance with nature, and belonging to household-management" (Aristotle 1981: 84). These are natural *chrēmatistikē*. However, there also exists a form of *chrēmatistikē* "associated with trade, which is not productive of goods in the full sense but only through their exchange." Aristotle here is referring to the purchase of goods and the reselling of the same goods at a profit – an act that creates monetary wealth without itself producing goods. Aristotle goes on to say that this type of *chrēmatistikē* "is thought to be concerned with coinage, because coinage both limits the exchange and is the unit of measurement by which it is performed;" that is, coin is both the input and output of trade, which is not true of fishing, barter or simple sale, where the input differs from the output. As the Athenian lawmaker Solon would have it, then, "there is indeed no limit to the amount of riches to be got from this mode of acquiring goods [*chrēmatistikē*]" and thus "is justly regarded with disapproval, since it arises not from nature but from men's gaining from each other" (Aristotle 1981: 84, 87).

Aristotle reserves his strongest disapprobation, however, for the practice of charging interest. He argues that this "dislike is fully justified, for the gain arises out of currency itself, not as a product of that for which currency was provided." He goes on to argue that "[c]urrency was intended to be a means of exchange (Aristotle 1981: 87; cf. Aristotle 1999: 75). Interest, however, "represents an increase in the currency itself." This "currency born of currency", then, "is the most contrary to nature" of all of the forms of exchange (Aristotle 1981: 87).

St. Thomas Aquinas

Aristotle exerted a strong influence on the thought of St. Thomas Aquinas, whose own condemnation of usury left its imprint throughout the economic thought of the Middle Ages (de Roover 1955). Aquinas took seriously Aristotle's contention that "currency born of currency" was unnatural, and so one finds in Question 78 of his *Summa Theologiae* the argument that taking "interest for money lent is unjust in itself, because this is to sell what does not exist, and this evidently leads to inequality, which is contrary to justice" (1998: 199). Aquinas continues, making explicit reference to Aristotle, in writing that "money, according to the Philosopher, was invented chiefly for the purpose of exchange," and therefore the proper usage of money "is its consumption or alienation, whereby it is sunk in exchange. Hence, it is by its very nature unlawful to take payment for the use of money lent...". Restitution, according to Aquinas, is therefore required in instances where money has been lent at interest:

"just as a man is bound to restore other ill-gotten goods, so is he bound to restore the money which he has taken in interest" (Aquinas 1988: 200).

Aquinas considered not only money but also credit under the rubric of interest-taking. Considering the practice common amongst Florentine merchants of deferring payment on goods for three months (a means facilitating trade), Aquinas writes in his "Letter on Credit Sales and Usury" that the merchant who sells his goods "for an amount exceeding the just price on account of his waiting for payment" engages in usury "inasmuch as the waiting for a certain time is included in the price" (1960: 223). Where the deferred payment is equal to the just price, no usury is committed (Aquinas 1960: 224). Consequently, for Aquinas, there could be "no moderate or just interest-taking; all interest-taking was usurious and usury was condemned, as was the usurer who endangered his immaterial soul" (Walsh 2004: 250). In Aquinas, then, one finds an Aristotelian argument against the taking of interest fused with Christian theology.[8]

David Hume

The themes running through the normative monetary thought of Aristotle and Aquinas – the role of money in exchange and the permissibility of particular financial practices – were recognised and further extended and adapted by the thinkers of the Scottish Enlightenment, most notably David Hume and Adam Smith. Hume, for example, recalls Aristotle's discussion of exchange in the opening of his essay "On Money" in arguing that money "is not, properly speaking, one of the subjects of commerce; but only the instrument which men have agreed upon to facilitate the exchange of one commodity for another. It is none of the wheels of trade: It is the oil which renders the motion of the wheels more smooth and easy" (1777/1889: 309). Hume goes on to present one of the first articulations of the quantity theory of money,

8. For a more detailed survey of medieval economic thought, including analyses of thinkers before and after Aquinas, see, e.g., Kaye (1998); Langholm (1979, 1992); Lapidus (1997).

writing that “the greater or less plenty of money is of no consequence; since the prices of commodities are always proportioned to the plenty of money” (1777/1889: 309). Should the money supply double, so too would the aggregate price level. Consequently, “it is of no manner of consequence, with regard to the domestic happiness of a state, whether money be in a greater or less quantity” (1777/1889: 315).

Hume, however, makes clear that he only believes the quantity theory to be true after a period of time has passed.[9] Continuing his discussion of money, he notes that “alterations in the quantity of money, either on one side or the other, are not immediately attended with proportionable alterations in the price of commodities.” Rather, these adjustments occur only slowly and unevenly: “There is always an interval before matters be adjusted to their new situation; and this interval is as pernicious to industry, when gold and silver are diminishing, as it is advantageous when these metals are encreasing” (Hume 1777/1889: 315). When the supply of money is decreasing (i.e., in the case of deflation), Hume states that

> The workman has not the same employment from the manufacturer and merchant; though he pays the same price for everything in the market. The farmer cannot dispose of his corn and cattle; though he must pay the same rent to his landlord. The poverty, and beggary, and sloth, which must ensue, are easily foreseen (Hume 1777/1889: 315).

Hume therefore recognised that the fundamental identity of the quantity theory of money did not provide a guide to short-term fluctuations, and that economic dislocation and harm to individual well-being were indeed the immediate results of a downward movement in the price level.

This concern with the harmful consequences of monetary phenomena is the root of Hume’s sceptical approach to banknotes. Hume admits that there is a commonly-held view that banknotes are beneficial to society because of their function in facilitating commerce. Though he recognises a societal preference for banknotes

9. Modern macroeconomists would say “in the long run.”

over bullion "as being of more easy transport and more safe custody", Hume nevertheless deems banknotes to be "a counterfeit money, which foreigners will not accept of in any payment, and which any great disorder in the state will reduce to nothing" (1777/1889: 311). Given a public preference for banknotes, however, Hume thinks it better to establish a "public bank" (i.e., a central bank) with the singular authority to issue paper money, as this would both channel the benefits of paper money to the state as well as prevent private bankers from manipulating the supply of banknotes for individual gain:

> A public bank, by this expedient, might cut off much of the dealings of private bankers and money-jobbers; and though the state bore the charge of salaries to the directors and tellers of this bank (for, according to the preceding supposition, it would have no profit from its dealings), the national advantage, resulting from the low price of labour and the destruction of paper-credit, would be a sufficient compensation. Not to mention that so large a sum, lying ready at command, would be a convenience in times of great public danger and distress; and what part of it was used might be replaced at leisure, when peace and tranquility was restored to the nation (Hume 1777/1889: 312).

Adam Smith

The interest in the relationship between monetary and financial practices and the public good that one finds in Hume is also apparent in the thought of Adam Smith, who also made a significant contribution to the tradition of normative monetary thought. As the founding figure of the classical political economy tradition, Smith has often been portrayed as a dogmatic defender of *laissez-faire* capitalism,[10] though a closer reading of Smith's most famous work, *The Wealth of Nations* (1776/1976), as well as his *Lectures on Jurisprudence* (1766/1978) reveals a more sophisticated thinker than

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10. This caricature, as common as it is, has little merit: a careful reading of Smith reveals the important exceptions he made to the general rule of economic liberty, the sum of which add up to a much larger role for the state in economic affairs than is conventionally appreciated. See Billet (1976); Heilbroner (1996: 104–105); Salter (1994); Verburg (2000).

the caricatures would suggest. One also finds that Smith has much to say about the normative implications of monetary and financial structures and practices.[11]

For Smith, economic liberty serves the purpose of advancing the good of society more than any other economic system (such as mercantilism, of which he was highly critical on positive and normative grounds). It is for this reason that Smith praised the growth of a money economy in Scotland – recalling both Aristotle and Hume in describing money as "the great wheel of circulation, the great instrument of commerce" that acts to "distribute to every man the revenue which properly belongs to him." Smith, however, breaks with Hume in his account of the proliferation of private banks that supplied banknotes and paper credit (1776/1976: 291). Smith observes that "the trade of the city of Glasgow doubled in about fifteen years after the first erection of the banks there; and the trade of Scotland has more than quadrupled since the first erection of the two publick banks at Edinburgh…". Though Smith does not regard this increase in economic activity as solely attributable to the establishment of the banks, "That the banks have contributed a good deal to this increase, cannot be doubted" (1776/1976: 297). "Hence the beneficial effects of the erection of banks and paper credit" were, for Smith, clearly an "advantage to the commerce of a country" (1766/1987: 503).

Smith also regarded having several banks in Scotland as being in the public interest, because competition amongst the banks impeded individual banks from overextending themselves (by keeping too little coin on hand to meet demands for redemption) and promoted caution:

> The only method to prevent the bad consequence arising from the ruin of banks is to give monopolies to none, but to encourage the erection of as many as possible. When several are established in a country, a mutual jealousy prevails, they are continually making unexpected runs

11. Most of Smith's moral philosophy is set out in his *Theory of Moral Sentiments* (1759/1976), though he did not consider issues of political economy at length in this text.

> on one another. This puts them on guard and obliges them to provide themselves against such demands (1766/1987: 505).

Smith goes on to argue that having several competing banks also mitigated the effects of bank failure should it occur, arguing that even if "one did break, every individual [would] have very few of its notes." Smith therefore concludes that "it is manifest that banks are beneficial to the commerce of a country, and that it is a bad police [sic] to restrain them" (1766/1987: 505-506).

Despite the emphasis on economic liberty in Smith's political economy clearly in evidence in these passages, he recognised that restraints on the liberty of some were necessary in particular instances to preserve both justice and the economic liberty of all (Billet 1976: 309–312). Chief among those few circumscribed areas where Smith would place checks on liberty are, in fact, banking and credit. Smith asserts that the activities of bankers are unique insofar as their pursuit of their self-interest (unlike the business of others) had the potential to frustrate the invisible hand, and that this prospect was sufficient justification for restraining their liberty (Armour 1976: 359–369).

This is the argument that emerges from Smith's reflections on the negative consequences of the growth of paper money. He observes that problems arose with the issuance of small-denomination notes. Where this was permitted, "many mean people are both enabled and encouraged to become bankers." While untrustworthy would-be bankers would have their five-pound or even twenty-shilling notes rejected by the public, their notes would be widely accepted when "issued for so small a sum as a sixpence." The "frequent bankruptcy to which such beggarly bankers must be liable," however, often meant "a very great calamity to many poor people who had received their notes in payment" (Smith 1776/1976: 323). Small-denomination banknotes, then, were open to abuse by unscrupulous bankers, and left the poor vulnerable to harm. As a consequence, Smith deems it justifiable to restrict the liberty of bankers by prohibiting such small-denomination notes. Smith concedes that such regulations "may, no doubt, be considered as in some respect a violation of natural liberty." Still, he argues that this particular exercise "of the natural liberty of a few individuals, which might endanger the security of the whole society" should nevertheless be "restrained by the laws of all governments." Smith goes on to say that such regulations are analogous to the "obligation of building party walls, in order to prevent the communication of fire," which is also "a violation of natural liberty," yet is well justified with reference to the protection of society (Smith 1776/1976: 324). A sound banking system, like sound building construction, was not compatible with unmitigated *laissez-faire*.[12]

Equally justifiable were laws proscribing the issuing of notes for which "payment was not exigible till several years after it was issued" and for which no interest was paid (1776/1976: 326). Smith attributes this practice to the governments of the British colonies in North America – Pennsylvania in particular – where government paper bearing no interest was issued and declared legal tender, yet was irredeemable for a period of fifteen years. Reflecting on this practice, Smith writes that to compel creditors to accept such notes "was an act of such violent injustice, as has scarce, perhaps, been attempted by the government of any other country which pretended to be free." Moreover, it smacked of "a scheme of fraudulent debtors to

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12. Smith also reflects on the societal impact of bank failures in discussing the case of the Ayr Bank in 1772, which had been established to provide credit to Scottish entrepreneurs at a time when the established Scottish banks were extremely conservative in extending credit, Smith notes that it "was more liberal than any other had ever been, both in granting cash accounts [i.e., lines of credit], and in discounting bills of exchange" – practices that would eventually lead to its collapse (Smith 1776/1976: 313). Smith's verdict on the failure of the Ayr Bank was that it allowed entrepreneurs "to carry on their projects for about two years longer than they could otherwise have done" but this "only enabled them to get so much deeper into debt, so that, when ruin came, it fell so much the heavier both upon them and upon their creditors." In hindsight, it "would have been much better for themselves, their creditors, *and their country*, had the greater part of them been *obliged to stop* two years sooner than they actually did" (1776/1976: 315; emphasis added). The overgenerous extension of bank credit, therefore, proved more harmful than helpful to society – and the Scottish government ought to have intervened earlier.

cheat their creditors" (Smith 1776/1976: 326). Smith therefore praised the act of parliament banning this practice (1776/1976: 327).

Also warranted, according to Smith, are laws limiting the legal rate of interest, "in order to prevent the extortion of usury," with the maximum legal rate of interest set slightly above the prevailing market rate (1776/1976: 356). The reason offered by Smith for strictly limiting the rate of interest that could be charged is that with a wide spread between the legal rate and the market rate, "the greater part of the money which was to be lent, would be lent to prodigals and projectors, who alone would be willing to give this high rate of interest."[13] As a consequence, "[s]ober people," meaning prudent, responsible entrepreneurs, "who will give for the use of money no more than a part of what they are likely to make by the use of it, would not venture into competition." So, "the capital of the country would thus be kept out of the hands which were most likely to make a profitable and advantageous use of it, and thrown into those which were most likely to waste and destroy it" (Smith 1776/1976: 357). It is important to note that Smith here speaks of limiting the rate of interest, not prohibiting any lending at interest, which was the counsel of Aquinas (as informed by Aristotle). Smith's view is that prohibiting lending at interest altogether not only choked commerce, but also served to "increase the evil of usury; the debtor being obliged to pay, not only for the use of the money, but for the risk which his creditor runs by accepting a compensation for that use" (1776/1976: 356). His concern is therefore with the effect of particular rules in directing capital into more (or less) socially advantageous endeavours.

What emerges from Smith, then, is a nuanced argument about both the helpful and harmful social consequences of particular financial practices and the justifiability

13. A "prodigal" in the eighteenth century referred to an individual who was wasteful or lavish in his or her spending – a squanderer. The term "projector", however, had a double meaning. It referred to one who plans or designs an enterprise or undertaking. It was also used in a term of derogation to refer to a promoter of bubble companies, a speculator, or a schemer. Smith appears to have the latter meaning in mind, but the double-meaning of "projector" plays a role in Bentham's critique of Smith discussed below.

of particular restrictions on individual economic liberty in the name of the greater good of society. Smith's ambivalence towards banking and finance, however, was not shared by his contemporary Jeremy Bentham, who saw a much smaller role for the state in bringing about socially beneficial financial outcomes.

Jeremy Bentham

In *A Defence of Usury* (1788), Bentham sets out to demonstrate the spuriousness of the grounds for what he sardonically calls "the barriers which law, either statute or common, have in their united wisdom set up … against the crying sin of Usury...". Against Smith, he argues "that no man of ripe years and of sound mind, acting freely, and with his eyes open, ought to be hindered" in his attempts to borrow; nor should "any body [be] hindered from supplying him, upon any terms he thinks proper to accede to" (Bentham 1788: 3). As for limiting the rate of interest to prevent the sort of prodigality that concerned Smith, Bentham writes that "[s]uch paternal, or, if you please, maternal care, may be a good work, but it is certainly a work of supererogation" (1788: 21). "There may be worse cruelty" committed by the state against its citizens than placing legal restraints on the rate of interest, Bentham admits, "but can there be greater folly?" (1788: 45).

Not only are restraints on the legal rate of interest "folly" for Bentham, they also do positive harm. Would-be borrowers could find themselves unable to find a willing lender at the highest legal rate of interest (Bentham 1788: 39–44). Legal restraints on the rate of interest, therefore "can not but do mischief" – the worst of which is "precluding so many people, altogether, from getting the money they stand in need of, to answer their respective exigencies." For Bentham, then, "the sole tendency of the law is to heap distress upon distress" (1788: 57–59). As well, restraints on usury further raise the cost of (illegal) lending. Lenders must be "indemnified, not only for whatsoever extraordinary risk it is that he runs independently of the law, but for the very risk occasioned by the law: he must be insured, as it were, against the law" (Bentham 1788: 67–68). This was a situation that Smith thought would not arise except in the case of a total prohibition on interest. Bentham, on the other hand, thought it might arise were there *any* limits on the rate of interest.

As for the "prodigals and projectors" that concerned Smith, Bentham writes that the number of prodigals "is too inconsiderable to deserve notice." Bentham also takes issue with Smith's disparaging references to projectors: he asks the reader "to consider, whether, of all that host of manufactures, which we both exult in as the causes and ingredients of national prosperity, there be a single one, that could have existed at first but in the shape of a project" (1788: 211, 217).

Bentham goes on to turn Smith's analysis against him in observing that "usury" already in fact occurs with the drawing and redrawing of bills of exchange: "In this way he [Smith] has shewn how money may be, and has been, taken up, at so high a rate, as 13 or 14 percent, a rate nearly three times as high as the utmost which the law professes to allow." So, "if usury is good for merchants," writes Bentham, "I don't very well see what should make it bad for every body else" (1788: 94–95).

Turning to the subject of how such usury laws came into being, Bentham argues that Christian teachings, anti-Semitism and an appropriation of Aristotle were combined to justify restraints on interest (1788: 121–130). In an argument foreshadowing aspects of Max Weber's *Protestant Ethic and the Spirit of Capitalism* (1904–5/1992), Bentham argues that Christian virtue "consisted in self-denial: not in self denial for the sake of society, but of self-denial for its own sake." The principle of right conduct that flowed from this understanding of virtue was "not to do what you had a mind to do; or, in other words, not to do what would be for your advantage." Thus, temporal advantage and spiritual advantage were "understood to be in constant and diametrical opposition." Further, it is getting money that "most men have a mind to do: because he who has money gets, as far as it goes, most other things that he has a mind for" (Bentham 1788: 123–125). Virtuous conduct understood as self-denial, then, proscribed borrowing.

As for lending, Bentham observes that to lend money at interest was seen as "acting like a Jew" – and "this Jewish way of getting it [money], was too odious to be endured. Christians were too intent upon plaguing Jews, to listen to the suggestion of doing as Jews did, even though money were to be got by it" (Bentham 1788: 126-127). This anti-Semitic view, however, did not stand on its own: "it found no unoppportune support in a passage of Aristotle" who "had established a despotic empire over the Christian world" (Bentham 1788: 127). Bentham writes of Aristotle that the

> great philosopher, with all of his industry ... had never been able to discover, in any one piece of money, any organs for generating any other such piece. Emboldened by so strong a body of negative proof, he ventured at last to usher into the world the result of his observations, in the form of an universal proposition, that *all money is in its nature barren*. (1788: 128).

For Bentham, this reliance on Aristotle to justify prohibitions on usury simply carried forward his faulty logic. In discussing Aristotle's argument, Bentham writes that it had not occurred to Aristotle that even though "a *daric* would not beget a daric, any more than it would a ram, or an ewe, yet for a daric which a man borrowed, he might get a ram and a couple of ewes, and that the ewes, were the ram left with them a certain time, would probably not be barren." The man could thereby profit from the resulting lambs: "if he sold his sheep again to pay back his daric, and gave one of his lambs for the use of it in the mean time, he would be two lambs or at least one lamb, richer, than if he had made no such bargain" (Bentham 1788: 130). In this carefully chosen example with natural reproduction at its centre, Bentham demonstrates the flaws in Aristotle's reasoning: currency serves more purposes than the simple exchange function Aristotle attributes to it. Money forms the basis of credit, which serves a facilitating role in commerce distinct from currency's use in exchange. In short, currency is not born of currency, but is rather born of its skilful use in commerce.

Thus, one finds in Bentham a stronger argument for individual liberty in the sphere of money and finance than one finds in Smith – the thinker most often regarded as *the* defender of economic liberty. *A Defence of Usury*, however, is silent on many of the banking practices that were attacked by Smith. Both the scope and extent of the disagreement between Smith and Bentham are therefore unclear.

John Maynard Keynes

With the shift from *political economy* to *economics* in the eighteenth and nineteenth centuries, a sharper distinction was drawn between normative and positive economic analysis; at the same time, positive monetary thought came to eclipse normative monetary thought. An important exception to this trend, however, is found in the monetary thought of John Maynard Keynes. For Keynes, economics was a *moral* science. Writing to Roy Harrod, Keynes asserts, *contra* Lionel Robbins (1932), who held that economists must maintain the clear distinction between positive and normative inquiry (and focus on the former), that “economics is a moral science and not a natural science. That is to say, it employs introspection and judgements of value” (Keynes 1938a: XIV, 297). Keynes was therefore highly critical of the “Benthamite tradition” of utilitarian political and economic thought on account of its “over-valuation of the economic criterion” in its analysis and for ignoring “the order and pattern of life amongst communities and the emotions which they can inspire” (1938b: X, 446, 449). For Keynes, therefore, economists’ most important task was to search out “new policies and new instruments to adapt and control the working of economic forces, so that they do not intolerably interfere with contemporary ideas as to what is fit and proper in the interests of social stability and social justice” (1925: IX, 306). Thus, Keynes’s life-long preoccupation was with “the quest for a liberal middle way between the harsh realities of economic competition and the stultifying embrace of egalitarian socialism” (Mead 2002: 204). Nowhere is this clearer than in his monetary thought.

An important theme in Keynes's monetary thought is the distribution of benefits and burdens within and between societies resulting from changes in the value of money – i.e., inflation and deflation. In opening his *Tract on Monetary Reform*, Keynes notes that "a change in the value of money, that is to say in the level of prices, is important to society only in so far as its incidence is unequal." These kinds of movements in the price level have "the vastest social consequences, because, as we all know, when the value of money changes, it does not change equally for all persons or for all purposes." A change in the value of money "affects different classes unequally, transfers wealth from one to another, bestows affluence here and embarrassment there, and redistributes Fortune's favour so as to frustrate design and disappoint expectation" (Keynes 1923: IV, 1).

For Keynes, these redistributive consequences of inflation and deflation were a matter of *justice*. Reflecting on the European financial tumult of the early 1920s, during which inflation benefited debtors at the expense of lenders and some wage-earners who actually saw increases in real wages, Keynes concludes that inflation has the effect of redistributing wealth "in a manner very injurious to the investor, very beneficial to the business man, and probably, in modern industrial conditions [where labour is organised], beneficial on the whole to the earner." However, for Keynes, the most distressing consequence of such inflation was "its *injustice* to those who in good faith have committed their savings to titles to money rather than to things" as an increase in prices entailed a reduction in the value of their savings (1923: IV, 29).

Deflation, in Keynes's view, had its negative consequences as well. Recalling Hume, Keynes's argument is that "falling prices means impoverishment to labour and to enterprise by leading entrepreneurs to restrict production, in their endeavour to avoid loss to themselves; and is therefore disastrous to employment." Also, just as inflation meant injustice to lenders, deflation meant the opposite – injustice to borrowers (Keynes 1923: IV, 36). But was there, according to Keynes, a lesser evil? While he thought that "both are evils to be shunned," deflation was the greater injustice: labour could better protect itself from overwork (associated with inflation) than from unemployment (associated with deflation). Weighing the alternatives, Keynes thought it "worse, in an impoverished world, to provoke unemployment than to disappoint the *rentier*" (1923: IV, 36).

Keynes's ideas on the just distribution of burdens arising from monetary adjustment were also embodied in his proposals for the rebuilding of the post-war international financial architecture. While Keynes had dealt briefly with international currency questions in his *Tract on Monetary Reform* (1923: IV) and *Treatise on Money* (1930: V–VI), he did not consider the topic at length until September 1941 when he wrote two Treasury memoranda: "Post-War Currency Policy" (1941a: XXV) and "Proposals for and International Currency Union" (1941b: XXV). In the former, Keynes rejected floating exchange rates and a return to the gold standard as sound foundations for the post-war international financial system. Keynes writes that the argument for floating exchange rates is "a doctrinaire delusion which disregards the lessons of historical experience without having behind it the support of sound theory" (Keynes 1941a: XXV, 21–22).

On the gold standard, Keynes argues that it has a deflationary bias, forcing the burden of downward adjustment on the debtor. Part of this argument is grounded in Keynes's positive monetary theory. He argues that "the classical theory that the unlimited free flow of gold automatically brings about adjustments of price-levels between the debtor country and the recipient creditor" must be rejected as it is founded upon "a crude and now abandoned quantity theory of money" which fails to account for the "lack of elasticity in the social structure of wages and prices" (Keynes 1941a: XXV, 27–28). But as his discussion in the *Tract* would suggest, Keynes's objection to the gold standard also has an important normative element:

> It is characteristic of a freely convertible international standard that it throws the main burden of adjustment on the country which is in the *debtor* position on the international balance of payments, – that is on the country which is (in this context) by hypothesis the *weaker* and above all

> the *smaller* in comparison with the other side of the scales which (for this purpose) is the rest of the world (Keynes 1941a: XXV, 27).

Later on the same memorandum, Keynes writes that "the contribution in terms of the resulting social strains which the debtor country has to make to the restoration of equilibrium by changing its prices and wages is altogether out of proportion to the contribution asked of its creditors" (Keynes 1941a: XXV, 28). Keynes therefore rejected a return to the gold standard as a foundation of the postwar international financial system because it functioned so as to "force adjustments in the direction most disruptive of social order, and to throw the burden on the countries least able to support it, making the poor poorer" (Keynes 1941a: XXV, 29).

From these remarks, it is clear that Keynes objects to the gold standard as a means of effecting balance of payments adjustment on account of the inequity resulting from its "normal" operation – that is, its failure to distribute the burdens of adjustment between debtor and creditor according to the ability of each to bear the resulting strains. Indeed, his placement of emphasis is telling: it is not simply that the burden of adjustment is borne by the debtor *per se*, but that it is the debtor as the weaker, smaller and poorer country that is compelled to adjust downwards. Keynes goes on to state emphatically the debtor is indeed compelled to adjust in a way that the creditor is not: "the process of adjustment is *compulsory* for the debtor and *voluntary* for the creditor." This is because "a country's reserve cannot fall below zero," yet "there is no ceiling which sets an upper limit [on reserves]" (Keynes 1941a: XXV, 28).

Keynes, however, qualifies his criticism of the gold standard by pointing approvingly to the London-centred international financial system of the late nineteenth century, which "transferred the *onus* of adjustment from the debtor to the creditor position" (Keynes 1941a: XXV, 21). During this period, "a flow of gold immediately translated itself, not in the first instance into a change in prices and wages, but into a change in the volume of foreign investment by the creditors...." This in turn "caused the burden to be carried by the stronger shoulders" (Keynes 1941a: XXV, 30). Keynes sees in the Victorian period an example to be emulated, and concludes that the architects of the post-war international order should be guided by the lesson that it offers: their aim should be to create a new international financial system which would "require the chief initiative [for balance of payment adjustment] from the creditor countries, whilst maintaining enough discipline in the debtor countries to prevent them from exploiting the new ease allowed them in living profligately beyond their means" (Keynes 1941a: XXV, 30). Keynes's vision for the post-war international financial architecture was thus one in which creditor and debtor alike would share the burden of balance of payments adjustment. Keynes sought to make this vision concrete in his International Currency Union (later International Clearing Union) proposal which formed the core of British proposals at the Bretton Woods conference (Keynes 1941b).[14]

Key themes in the history of normative monetary thought

This foray into the history of political economy makes clear that there exists a rich tradition of inquiry into the ethical implications of monetary and financial structures and practices – a tradition I refer to as normative monetary thought. Though certainly plural in terms of the perspectives on money and finance represented within it, a number of unifying themes emerge from this survey of the history of normative monetary thought.

The first key theme is the recognition (albeit implicit) that money and credit – as well as the social practices governing access to them and their use – constitute part of the *basic structure of society*. According to John Rawls, the basic structure of society includes "the major social institutions [that] distribute fundamental rights and duties and determine the division of advantages from social cooperation." These institutions

14. See also Harrod (1951: 525–585); Moggridge (1992: 670–694); Skidelsky (2000: 179–232).

include "the political constitution and the principal economic and social arrangements." The basic structure exerts a significant influence over individuals' "life prospects, what they can expect to be and how well they can hope to do" (Rawls 1971: 7). This history of normative monetary thought makes clear that money and finance fit this definition of the basic structure of society.

Beginning with Aristotle, one sees recognition of the critical role of money in facilitating economic exchange. Aristotle writes that "all items must be comparable in some way. Currency came along to do exactly this" – and the potential for mutually-beneficial exchange would be seriously reduced without it. Indeed, Aristotle goes so far as to say that "there would be no community without exchange" (Aristotle 1999: 75–76). Similar views of money are found in Hume (1777/1889: 309), who called money the oil that allowed the wheels of trade to turn, and the socially-agreed instrument for economic exchange. Smith's view follows Hume closely, where money is similarly described as essential to commerce (1776/1976: 291). There is, therefore, a shared (but latent) understanding that individual life opportunities would be seriously frustrated in the absence of money – goods would be incomparable, and the wheels of trade would begin to grind. From Aristotle onwards, therefore, monetary and financial structures and practices were recognised as forming part of the basic structure of society. As such, they constitute important objects of normative analysis.

Equally important as money's role as a means of exchange and unit of account is its role as a store of value – in particular, *changes* in the value of money – in affecting individual life opportunities. To revisit aspects of the discussion above, Hume writes of the "poverty, and beggary, and sloth, which must ensue" from deflation (1777/1889: 315). Keynes similarly argues that "falling prices means impoverishment to labour and to enterprise" while also noting the injustice committed against savers by inflation (1923: IV, 29, 36). Both upward and downward movements in the price level, therefore, were understood to cause real harm. Keynes is clear: both inflation and deflation are *evils*. As well, one ought to recall Smith's discussion of bank failures (which obviously entail a sudden reduction of the value of money to zero) as representing "very great calamity" whose effects are borne disproportionately by the poor (1776/1976: 323).

Though the observation that money and finance constitute part of the basic structure may not appear to be especially insightful to those working within political economy framework, it is important to recognise that contemporary political theory fails to admit such a role. In discussing the basic structure, Rawls discusses income and wealth as two of the primary social goods that the basic structure functions to distribute, though he goes on to refer to the "*stock* of benefits" and "collection of *goods*" to be divided (Rawls 1971: 62, 88; emphasis added). Rawls's defence of his famous difference principle frames the question of social justice in terms of its application in allocating money and other resources (Rawls 1971: 150-161). He does not extend his discussion to consider the application of the difference principle to the economic processes that *themselves* function to allocate and redistribute money.

This neglect of money and finance is also evident in Rawls's conception of an economic system. He writes that an economic system "regulates what things are produced and by what means, who receives them and in return for which contributions, and how large a fraction of social resources is devoted to saving and to the provision of public goods" (Rawls 1971: 266). Money and credit, therefore, appear to have little place in Rawls's ideal of an economic system. What is missing from the above description of an economic system is how financial capital (i.e., credit) enables production, to whom credit is made available, and at what cost.

One also sees this neglect in Charles Beitz's extension of Rawls's thought. In Beitz's theory of global distributive justice, one finds a recognition that global finance constitutes part of an "evolving global basic structure" (1979: 202), though Beitz fails to articulate principles of justice for a globalised financial system as part of ideal theory. His central concern remains the distribution of natural resources, and he does not extend his discussion of the kinds of redistribution required by a global difference principle beyond a vague prescription for larger inter-state transfers of wealth (1979: 137–141, 153). Beitz's conception of the basic structure is also incomplete, and as a consequence so is his theory of global distributive justice. Contemporary (international) political theory, then, has yet to absorb the lessons the history of normative monetary thought has to offer.

One such lesson is the need to consider distributive justice of a particular sort: not the distribution of money and financial resources as such, but the distributive (or maldistributive) effects of phenomena that *act on* money and credit – such as inflation and deflation, bank failures, and the expansion and contraction of credit. This is a particular *dynamic* conception of distributive justice.

Another recurring theme in the history of normative monetary thought is the permissibility of interest-taking, or put differently, the permissibility of the particular terms upon which credit is extended. Aristotle, Aquinas, Smith and Bentham give different answers to this question. Beginning with Aristotle and Aquinas, credit practices were recognised as part of commercial activity, but the specific practice of lending at interest was judged unnatural and therefore proscribed. Though influenced by ancient and medieval thought, Smith moved towards acceptance of interest-taking in advocating for legal limits on the rate of interest, not an outright ban on lending at interest. Smith recognised the importance of credit to economic growth in contemporary Scotland, which would have been seriously retarded in its absence. As well, Smith recognised that would-be borrowers could not appeal to the benevolence of would-be lenders (cf. Smith 1776/1976: 26–27), and so some payment for the use of money would be exigible, though this ought to be limited by law. Bentham, however, rejected any such limits on the rate of interest on both positive and normative grounds. The history of normative monetary thought, therefore, does not provide a unified answer to the question of credit practices, though it highlights the importance of normative theorising about credit and the practices governing its use.

The exchange between Smith and Bentham also points to another theme in the history of normative monetary thought: the tension between individual liberty and the greater good of society. This is a theme that obviously runs throughout modern political thought, though for Smith and Bentham, discussion of this theme takes place within the context of a broader discussion of money and finance. One should of course note that in debating the legitimate role of the state in monetary and financial affairs, Smith and Bentham give equal place in their arguments to what is *right* and *legitimate* as what is *efficient*.

To conclude, the history of normative monetary thought contains numerous intellectual resources useful in theorising the "middle void" between the global finance and global justice literatures. Thinkers from Aristotle to Keynes have contemplated the ethical character of particular monetary structures and practices, giving particular attention in their analyses to the place of money in the basic structure of society, the distributive (or maldistributive) effects of inflation and deflation, and the ethics of credit. In thinking through the requirement of justice in the context of globalised finance, then, we would do well to remember Keynes's dictum: "A study of the history of opinion is a necessary preliminary to the emancipation of the mind" (1925: IX, 305).

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