ADAM SMITH'S ACCOUNT OF SELF-DECEIT AND INFORMAL INSTITUTIONS

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Abstract

According to Adam Smith, self-deceit is essential to the economy. In this light the paper draws on the *Theory of Moral Sentiments* and revisits Adam Smith’s view of the self. The originality of Smith’s account of self-deceit is seen in his insights into self-regulating social forces. The paper illustrates how, in this view, informal institutions are important because they countervail self-deceit in markets. It suggests that Smith overestimated these countervailing forces for the reason that informal norms are also able to amplify self-deceiving agents.

*Key words:* self-deception, self-love, sympathy, informal norms, self-regulation, positive and negative feedback.

JEL Classification System: B 12, B 31.
0) Introduction

There was scarcely another author in the 18th century who wrote more on self-deception than Adam Smith (Fleischacker 2004, 51). But this is not well known to economists, who routinely attribute to him the view of agents relentlessly pursuing their self-interest. The individual desire to acquire wealth typically associated with the pursuit of self-interest is exemplified in Smith’s foundational treatise on the nature and the causes of national wealth ([1776]1997), whereas the individual tendency to self-deceive figures more prominently in Smith’s philosophical analysis of The Theory of Moral Sentiments ([1759] 2001).

Unfortunately Adam Smith failed to pronounce explicitly on the relationship between the two works (in other words the relation between economics and ethics). This has also nourished the infamous Das Adam Smith Problem, the debate among Smith scholars exploring the relationship, or better still, the absence of a relationship between his economic and his non-economic work. Against this background, the present analysis focuses on a relationship between the two books on which Adam Smith was explicit, namely his suggestion that self-deceit has an economic impact. While Smith established the relationship between self-deceit and economics in his non-economic work, his emphasis on its economic relevance at the same time indicates a link between his economic and philosophical analyses. It is in the latter that Smith is explicit about how economic activity may well depend on self-deceive. In Smith words, self-deceit “roused and keeps in continual motion the industry of mankind” (183). Hence self-deceit motivates

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1 According to Fleischacker, there is no more detailed investigation of self-delusion (apart from Bishop Butler’s sermons) in 18th century moral philosophy (2004, 51).

2 Although the self-interest hypothesis as it is used in economic theory today does not in principle exclude non-material or non-monetary goals, it is clear that economic freedom as understood in the standard view and as it is conventionally attributed to Adam Smith relies on the axiom that “individuals desire to maximize their wealth” (Rashid 1992,149). Also the individual tendency of self-deceit is not absent from Smith’s economic work, but for an analysis of its foundations we need to refer to his non-economic work.

3 Adam Smith in the traditional view has become a representative of the modern divide between economics and ethics. For an overview of the various stages of the scholarly debate in relation to Das Adam Smith Problem since its inception in 19th century Germany see also Montes (2003). The discussion has not yet reached a definite solution according to Montes (2003, 81). One important aspect of the ongoing debate is whether economics needs a re-entry of (civil) ethics. There is a recent resumption based on Smith’s moral theory that argues in favour of this new orientation. Drawing on Sen’s contributions to ethics and economics, Evensky (2005, 245ff) and also Montes (2003, 86-7) are cases in point. Consequently in a recent essay entitled “Adam Smith’s Economics”, Sen and Rothschild (2006) draw on Smith for a broader use of the concept of rationality as a “sociable and discursive condition” (362) in the sense of being able “to evaluate means and also ends” (362). Accordingly, in his historiographical account of Das Adam Smith Problem Dickey (1986) makes the claim that in his final version of the Theory of Moral Sentiments Smith made clear that a moral self is needed in order to reconcile commerce and civil progress. Whether one adopts such a view or not, the problem seems to remain that two books exist that in principle could also have been written by two different authors. Smith did not make any explicit connection between them. And inconsistency between them probably remains at many levels. Also as Vivienne Brown (1994) correctly emphasizes, at the level of textual analysis at least, Smith led dissimilar discourses, a moral one in The Theory of Moral Sentiments and an amoral one in The Wealth of Nations.

4 The following quote on the motivational force reads “it is deception which rouses and keeps in continual motion the industry of mankind” (Smith [1759] 2001, 183) and although Smith uses the term “deception” in this context, it is clear that this involves mainly self-deceit.
economic activity. In other words, self-deceit motivates man to work, to consume and to invest.\(^5\)

In contrast to the economic importance of self-deceit emphasized by Smith in *The Theory of Moral Sentiments*, economists are not normally interested in this human trait. First, in the light of the prevailing rationality assumption in economics, the thought of a self-deceiving person does not make much sense. Such a person is clearly ‘irrational’ and not included in standard behavioural assumptions. Typically, self-deceit is seen as incompatible with the economic approach to human behaviour.\(^6\) And second, when seen from the market view, self-deceit is regarded as unimportant, because it is assumed (albeit often implicitly) that in markets ‘irrationalities’ such as this human tendency will not survive.\(^7\) Self-deceiving agents will be eliminated by market forces\(^8\), since markets are supposed to punish them and beat them into shape, or if this is impossible, eliminate them altogether.

The present paper examines Smith’s account of self-deceit. It shows that in this account human self-deceit is not always countervailed by market forces because it also depends on informal institutions. By drawing on Smith’s non-economic work it illustrates how informal institutions may contribute to the amount of self-deceit in markets. The present analysis claims that such institutions may both countervail and amplify self-deceit.

In the assertion cited above, Smith seems to suggest that if people were perfectly ‘rational’, stagnation would result. Whether this is correct or not remains a moot point, but what his suggestion nonetheless implies is that in contrast to the economic view, human self-deceit and economic functioning are not completely unconnected. The present paper also puts forward a possible new connection between Smith’s economic and philosophical analysis, the nature of

\(^5\) According to Smith self-deceit “first prompted… [man] … to cultivate the ground, to build houses, to found cities and commonwealths, and to invent and improve all the sciences and arts, which enoble and embellish human life; which have entirely changed the whole face of the globe, have turned the rude forests of nature into agreeable and fertile plains, and made the trackless and barren ocean a new fund of subsistence, and the great high road of communication to the different nations of the earth” (Smith [1759] 2001, 183-4).

\(^6\) Caplan adopts an opposite view and aims at reconciling self-deception (i.e. collective illusions in terms of false religious and political beliefs) and the economic approach to human behaviour (1999; 2001). However, while he reconciles rationality and self-deceit at the individual level, he also confirms the market view that due to countervailing forces, self-deceit is inessential in markets because of the disincentives associated with them. Alternatively, from the perspective of psychology and economics, recent preoccupations have also focused on the rationality of self-deception (Tirole 2002; Bénabou and Tirole 2002) and on its economic consequences (Carrillo and Mariotti 2000). Akerlof pioneered this research in studying the economic consequences of people choosing beliefs that make them feel good about themselves (Akerlof [1982]1998) and people with a hedonic concern for self-image in the form of preferences over beliefs (Akerlof and Dickens 1984). Akerlof, however, does not analyse self-deceit in markets (but refers to self-deceit in businesses and public policy where incentives for unbiased use of information are absent).

\(^7\) For some observations on the traditional economic view of the irrelevance of behavioural irrationalities in markets see Fehr and Tyran (2005).

\(^8\) An example of this market view to which Smith referred in his *Wealth of Nations* can be seen in his insight into how the commerce of the town contributes to the improvement of the country. He cites the example of the noble landlords, who traded their power away in “the wantonness of plenty, for trinkets and baubles, fitter to be the play-things of children than the serious pursuits of men” ([1776]1997, Vol. 1, 421). The self-deceiving landlords (acting against their own interests on account of self-deceit motivated by vanity) are finally eliminated by countervailing market forces. In his essay on Smith’s view of man, Coase (1976) implicitly suggests that Smith’s metaphor of the invisible hand (which he interprets in evolutionary terms) should also be seen in terms of countervailing forces to self-deceit. The invisible hand, he claims, solves the problem of how individuals who live “in a world of self-delusion” (12) in Smith’s view can bring about natural harmony, and perhaps more importantly, can be off-set by “social benefits” (17).
which has also inspired Das Adam Smith Problem. Two positions can be roughly identified regarding the relation between Smith’s economic and philosophical analyses. The traditional position claims that Smith’s analysis in his Theory of Moral Sentiments is deficient in terms of economic analysis (Grampp 1948, Hollander 1977, Viner 1927)⁹, while the more unconventional position holds that Smith’s economic analysis is deficient if separated from his philosophy (Evensky 2005a).

The connection made between The Wealth of Nations and The Theory of Moral Sentiments by way of self-deceit that is suggested here is, I believe, valid for both positions. The present paper focuses on a specific connection between the two books: namely Smith’s assertion in the Theory of Moral Sentiments which – in contrast to the economic view outlined above – suggests that self-deceit can have economic implications, and hence should also be relevant from an economic point of view.

The paper is organized as follows. The first section selectively refers to the philosophical discussion of self-deceit in Adam Smith with a view to delimiting the focus on informal institutions adopted here. The second section presents Adam Smith’s inquiry into the nature and causes of self-deception in relation to basic concepts in his Theory of Moral Sentiments. The basic concepts are self-love and sympathy, and their relation to self-deceit is discussed in that order. Section three examines sympathy and its relationship to Adam Smith’s insights on the self-regulation of society and informal institutions. Drawing on Smith’s insights into informal institutions, sections four and five show examples of how self-deceiver is either constrained or reinforced. The conclusion returns to Smith’s claim that self-deceit is relevant to the economy.

1) The philosophical discussion of self-deceit in Adam Smith

Scholars who have focused on Adam Smith the economist have rarely been interested in what he has to say on self-deceit. Moreover, among scholars who have given priority to Adam Smith the moral philosopher, few have also explicitly dealt with Smith’s account of self-deceit. They are not so much interested in whether self-deceit has economic implications or not (this is often taken for granted by these scholars), but on whether economic growth based on self-deceit in Smith’s view entails man’s moral corruption or not. These interrogations on self-deceit are classic examples of moral philosophy, which regards self-deception as dangerous because it leads to wrong moral judgements, hence corrupting a man’s conscience.

In the traditional view, Smith’s suggestion that economic development depends on self-deceit would have entailed seeing the economy (and in what Smith also declared to be the prior economic motivation, namely the pursuit of wealth) as a form of moral corruption. When regarded in this light, economic and moral development are incompatible, and these scholars were interested to find out how Smith, as a moral philosopher, could have given priority to man’s economic motivation at all. Also recalling Das Adam Smith Problem ¹⁰, to which these

⁹ These authors see in The Wealth of Nations “his most mature work” (Grampp 1948, 317) in which Smith has given up his “romanticism” (Viner 1927, 2001). Before the “pathetic political man” (Grampp 1948, 330) of The Theory of Moral Sentiments “was [not] pushed aside by a calculating individual” (330) a more “plausible and useful explanation of economic activity was unlikely if not impossible” (321).

¹⁰ The question whether the economic development Smith advocates spoils morality or not can also be seen as a specific version of Das Adam Smith Problem (which as the ongoing debate shows) has remained unsolved to date (cf. also footnote 3 above).

But not all scholars recognize it as a problem. Evensky, for example, claims that there is no Adam Smith Problem (2005, 22). In his view, one general motivation reveals itself in both his economic and his non-economic work, namely “humankind’s progress” (2005, 38). While tendencies to eliminate the problem by way of positing one common vision exist, I believe that Pack (1997) and also Ottenson (2000) were right that this larger vision cannot completely overcome the tension between the two books, hence their scepticism in relation
scholars might have added a new version, they asked whether Smith’s view of self-deceit in an economic context was consistent with his moral philosophy or whether it undermined civilization and progress (Griswold 1999). On the one hand, it has been suggested that self-deception, while facilitating economic development, would hinder moral and social development (Streminger 1995). While for Streminger self-deception is clearly a hindrance to man’s striving for moral perfection (202ff) and therefore conflicts with Smith’s approval of it, for Griswold on the other hand, self-deceit does not necessarily entail moral corruption because in a free commercial society it is likely to be countered by “moral education, habitation in moral rules, and a reasonable arrangement of social institutions and life” (1999, 225). After all, he says, a free commercial society is not opposed to virtues and moral rules but should rather be understood as supporting their further propagation. Schliesser (2006, 348ff) adds that for Smith the social reformer, whose emphasis was on correct institutions, the endorsement of self-deceit in his natural system of liberty was no contradiction to morality (in contrast to Rousseau) because for him prosperity and wealth were at the foundation of freedom and independence.

It is important to note that an economic examination of self-deceit is different from a philosophical one, possible interdependences notwithstanding. Traditional moral philosophy has seen in self-deceit a hindrance to progress and the further improvement of mankind; modern scholars approach this question differently. They do not pit the pursuit of virtue and economic drives against each other, but make obvious how the very pursuit of riches or the drive to “better our condition” (Vol.1, 341), as Smith called it in The Wealth of Nations, is compatible with humanity’s civil progress. Fleischacker (2004, 104-18), who claims that a philosophical view of Adam Smith should be adopted, is a typical example of this account. He aims at reconciling the moral and the economic realms. According to him, there is no contradiction between homo moralis and homo economicus, because to be able to thrive, the former necessarily depends on the latter. In other words, one can perfectly well pursue wealth and be a decent fellow at the same time.

According to Fleischacker’s analysis of Smith’s economic contributions, therefore, Smith’s assertions about the economic implications of self-deceit amount to a “moralistic fairy tale” (2004, 111) and are unimportant for his economic analysis. In Smith’s economic analysis, this is what Fleischacker seems to imply: there is no need to consider self-deceit because it is “inessential” (114).

However, Smith’s claim that self-deceit is essential to the economy is different from the claim that self-deceit in the economic context may finally be a good thing from the point of view of moral philosophy. In contrast to Fleischacker, Griswold’s insistence that for Smith self-deceit

to an appropriate solution of the problem. Here I also agree with Brown’s emphasis on the insurmountable tension between his two books (1994). I believe that it is this tension that has also inspired the alternative claims regarding Smith’s legacy, pitting “Chicago Smith” and “Kirkaldy Smith” against each other (Evensky 2005a, 245-64). In an earlier analysis, Macfie ([1955]1967) also develops the contrast between two legacies in economic thought, the “English” (22) and the “Scottish” (19) legacy. For him, Adam Smith is representative of the “the Scottish attitude and method”, which is “more concerned with giving a broad well balanced comprehensive picture seen from different points of view than with [the] logical rigour [of the former]” (22).

In any case, if we adopt the point of view of modern economics, which is in the “British” (Macfie), or the “Chicago Smith” tradition (Evensky), Das Adam Smith Problem is inexistent. It should be recalled that the economics canon welcomes the fact that economics has put its foundations aside and separated from moral philosophy. According to Brown, it is one of the greatest ironies of all that Adam Smith’s discourses, which were as she makes clear so much indebted to moral philosophy, have contributed crucially to this current situation (1994, 220).
stimulates economic growth\textsuperscript{11} also suggests that in addition to the philosophical interest, self-deceit is of economic interest. Hence it is clear that Smith’s “deception theory” (Macfie 1967, 61)\textsuperscript{12} is not only suited for philosophical examination, and the present paper puts the stress on the economic insights it may reveal.

According to the standard economic view outlined in the introduction, the rationality assumption at the heart of economic analyses usually excludes self-deceit. In this light, the next section revisits Adam Smith’s view of the self. This account is to be understood in the light of two basic principles, namely self-love and sympathy (Force 2006, 324; Gerschlager 2005) and this is why the nature and causes of the human tendency to self-deceive will be discussed in the light of these. In contrast to the economic view, Smith took on a lot with this human tendency. After all, according to him it was the starting point of “half the disorders of human life” ([1759] 2001, 158).

2) Adam Smith’s concept of the self: the nature and causes of self-deceit

a) Self-love and self-deceit

In his Theory of Moral Sentiments Adam Smith attempted to provide a new foundation for social order based on the individual. The individual agent relentlessly pursuing his self-interest is regularly attributed to him. According to Smith, there can be little doubt that among all motives, self-love is to be considered as prior.

“Every man is, no doubt, by nature, first and principally recommended to his own care; and as he is fitter to take care of himself than of any other person, it is fit and right that it should be so. Every man, therefore, is much more deeply interested in whatever immediately concerns himself, than in what concerns any other man” ([1759] 2001, 82-3)... …[he] feels his own pleasures and his own pains more sensibly than those of other people. The former are the original sensations; the latter the reflected or sympathetic images of those sensations. The former may be said to be the substance; the latter the shadow” ([1759] 2001, 219). The picture conjured up by Adam Smith’s discussion in the Theory of Moral Sentiments is that of man immersed in self-love. “We are not ready,” he says, “to suspect any person of being defective in selfishness” ([1759] 2001, 304).

And yet, for Smith, this prior concern for oneself is only natural; it is not to be seen in terms of opportunism [Williamson 1985], with which the notion of self-interest has become mostly associated. In his analysis on the connotations of the concept of self-love, Force (2006) has shown that Smith even rejected the selfish hypothesis that was later associated with self-
interest. Self-love or self-interest, two notions that Smith uses interchangeably throughout his works, do not denote an unsocial character per se, but rather that the concern for oneself is regarded as sound and healthy, because a necessity. “Individuals are recommended by Nature” to their “care and attention” (Smith [1759] 2001, 219). The alternative would be neglect and abandonment, and man would not be able to survive in the first place. Self-love as such is also seen as neutral in moral terms: it is neither a virtue nor a vice, but can give rise to both depending on the tastes and character of men.

When we take a closer look at his *Theory of Moral Sentiments*, we also realize that self-love and self-deceit depend on each other, because in Smith’s view much self-deceit finds its cause in self-love, or more precisely, in an excess of it. As seen by Smith, self-deceit therefore has primarily a motivational source.

Smith develops a portrait of man indulging in self-love and consequently deluding himself. According to him, we all tend, because it is agreeable, to think more highly of ourselves than is really justified. And “we are,” Smith continues, “all naturally disposed to over-rate the excellencies of our own character” ([1759] 2001, 133). The problem is that it “is so disagreeable to think ill of ourselves, that we often purposely turn away our view from those circumstances which might render that judgment unfavourable. Claim He is a bold surgeon, they say, whose hand does not tremble when he performs an operation upon his own person; and he is often equally bold who does not hesitate to pull off the mysterious veil of self-delusion, which covers from his view the deformities of his own conduct. Rather than see our own behaviour under so disagreeable an aspect, we too often, foolishly and weakly, endeavour to exasperate anew those unjust passions which had formerly misled us” ([1759] 2001, 158). According to Smith, self-love becomes distorted when there is an excess of it. As a consequence, men often also make fools of themselves. And vanity for Smith is a case in point.

Smith typically associates human self-deceit with his partiality both at the time of action and after it. First, when “we are about to act the eagerness of passion will seldom allow us to consider what we are doing, with the candour of an indifferent person. The violent emotions which at that time agitate us, discolour our views of things; even when we are endeavouring to place ourselves in the situation of another, and to regard the objects that interest us in the light in which they will naturally appear to him, the fury of our own passions constantly calls us back to our own place, where every thing appears magnified and misrepresented by self-love. Of the manner in which those objects would appear to another, of the view which he would take of them, we can obtain, if I may say so, but instantaneous glimpses, which vanish in a moment, and which, even while they last, are not altogether just. We cannot even for that moment divest ourselves entirely of the heat and keenness with which our peculiar situation inspires us, nor consider what we are about to do with the complete impartiality of an equitable judge. The passions, upon this account, … all justify themselves, and seem reasonable and proportioned to their objects, as long as we continue to feel them” ([1759] 2001, 157].

The second instance of self-deceit according to Smith is when the action is over “and the passions which prompted it have subsided … we coolly enter into the sentiments of the man within. What before interested us is now become almost as indifferent to us as it always was

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13 According to Force (2006), the association of self-love with self-interest in the sense of selfishness in Adam Smith is also a result of a misreading of the French translation in the 19th century through which many economists became acquainted with his ideas.

14 Witztum (1998, 491) and Coase (1976, 24) in different contexts and with a different perspective both claim that there is an association between self-interest and self-deception in Adam Smith.
to him, and we can now examine our own conduct with his candour and impartiality. The man of to-day is no longer agitated by the same passions which distracted the man of yesterday: and when the paroxysm of emotion, in the same manner as when the paroxysm of distress, is fairly over, we can identify ourselves, as it were, with the ideal man within the breast, and, in our own character, view, as in the one case, our own situation, so in the other, our own conduct, with the severe eyes of the most impartial spectator. But our judgements now are often of little importance in comparison of what they were before; and can frequently produce nothing but vain regret and unavailing repentance; without always securing us from the like errors in time to come. It is seldom, however that they are quite candid even in this case. The opinion we entertain of our own character depends entirely on our judgements concerning our past conduct. It is so disagreeable to think ill of ourselves, that we often purposely turn away our view form those circumstances which might render that judgement unfavourable … we endeavour by artifice to awaken our old hatreds, and irritate afresh our almost forgotten resentments: we even exert ourselves for this miserable purpose, and thus persevere in injustice, merely because we once were unjust, and because we are ashamed and afraid to see that we were so” ([1759] 2001, 157-8).

The idea of self-deceit Smith conveys here is that people are taken in by their passions. Smith explains that the “man of furious resentment” (160) who listens to the dictates of that passion, “would … regard the death of his enemy as but a small compensation for the wrong, he imagines, he has received; which, however, may be no more than a very slight provocation” (160). The selfish passions are sufficient to induce oneself to make “a very different report of what the real circumstances of the case were capable of authorizing” ([1759] 2001, 157). In this light, the furious resentment that dominates man in the moment of action is one example of what we will call here a foolish motivation, and, as Smith shows, it may be regretted after the action. For example, Smith refers to “horrors of shame and repentance” that are associated with sanguinary revenge ([1759] 2001, 161). And yet, he understands that self-deceit often persists after the action, because people do not want to think ill of them.

Our disposition to “over-rate the excellencies of our own character” may well result in the motivated manipulation of our beliefs where it “colours our perception of the outcomes of alternative courses of action” (Coase 1976, 24). In addition, in Smith’s view the same disposition also accounts for the motivated pursuit of foolish ambitions. Self-deceit “exasperate[s] anew those… passions which had formerly misled us” as Smith made clear ([1759] 2001, 158). While the former suggests motivated beliefs about the future states of the world, the latter suggests motivated values and preferences (or motivations) that might mislead the individual.

What is really at stake to my mind in Smith’s view of self-deceit is the nature of human ambitions. Smith suggests that the individual evaluates his values and preferences. The focus of the examples selected in the present paper is therefore on human ambitions, i.e. the fact that human beings are (and indeed are often eager) to pursue foolish ambitions.

When self-deception is a constant companion, as Smith believed, humans cannot perceive information without any biases nor can they always be believed to be accurately informed about what they want. The motivational priority of self-love does not save the individual from being mistaken about both his beliefs and his motivations. This insight also qualifies the standard claim about the self that is regularly attributed to Adam Smith, that the self-interested agent always knows best what these interests are. The knowledge assumption implied in this claim seems to be very much in contrast to Smith’s insights into self-deceit.
The individual self in Smith’s view is less sure of herself and less perfectly aware of what she wants than the standard assumption of self-interest usually assumes.\(^\text{15}\) Smith knew of the limitations of human reason due to self-deceit, which, according to him, was next to irresistible, as the analogy with the surgeon above indicates. The picture Smith depicts of self-love is much more ambivalent than economists, who have often preferred to stress the virtuous aspect of this motivation (namely self-interest in the sense of prudence), have traditionally acknowledged.\(^\text{16}\)

**b) Sympathy**

In addition to self-love (and hence self-deceit), the second basic concept of Smith’s account of the self is sympathy ([1759] 2001, 9). The concept of sympathy is crucial, because it allows the individual to extend beyond her own place and circumstance. It is what in Smith’s view constitutes living in a society. Smith’s concept of sympathy also provides the foundations for a new understanding of social order in which individuals are urged to pursue their own interests in the first place.

A number of meanings have been attributed to sympathy and the present section will discuss the most important of these with a view to clarifying how the concept as used here is able to reveal insights into self-deceit.\(^\text{17}\) To this end sympathy is seen as the weakest of all senses that have been associated with it. In the weakest sense in which Smith’s use of sympathy can be understood it refers to what in modern parlance would be denoted by the term “empathy” (Fontaine 1997, 263).

Sympathy in this sense has all the characteristics of an imaginary exchange, or more precisely perhaps, an exchange of places in the imagination (Gerschlager 2001; 2005). When Smith talks about the foundations of social order, he has also in mind an empathic exchange of circumstances in the imagination. He actually used the term “change” to denote an exchange of “persons and characters” ([1759] 2001, 317). Exchange and change are interchangeable here since change in his day was used in contexts where in modern English exchange or interchange would be used (in the sense of “to give and receive reciprocally”). This use survives in expressions such as “to change places” (The Oxford English Dictionary, 16). Experiencing sympathy involves imagination. By means of the imagination we can feel what

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\(^{15}\) In Smith’s view it would ask too much of the individual to be always perfectly informed about what she wants. In this view, the dictum that [self-] “interest will not lie” (cf. Gunn 1968; cf. Suttle 1987, 464), which is at the foundation of standard economic models of *homo economicus*, would need to be put into perspective. Some of the foolish individuals to whom Smith refers virtually act against their self-interest, such as the landlords who trade their power away for nothing ([1776]1997, Vol. 1, 421). According to Macfie the concept of self-love implied the notion that one could be mistaken (about one’s needs and nature) in contrast to a later adopted idea that what a person felt represented the interest of his self and was necessarily his true self-interest (1967, 80). In addition Smith’s individual is not “rational” in the sense that she corresponds to some precise axioms, as recent analyses of cognitive biases in the sense of distortions from expected utility theory have also shown (Ashraf et al. 2006). I do not analyse in greater detail the relation between rationality (in the sense of rational choice) and self-deceit in this paper.

\(^{16}\) According to Witztum (1998, 491) self-interest interpreted as prudence has been a major theme in present-day readings of Smith. In these readings self-interest is focused on in terms of prudence and includes ethical concerns for unselfish charitable ends or benevolence. A different perspective on Smith is adopted by Khalil (cf. Khalil 1996; Khalil 2006, 10-1) and his focus on the vicious aspects of what he calls ‘egocentric human motivations cherished by modernity’.

\(^{17}\) Smith’s concept of sympathy is a thorny problem and its re-examination has been a major issue in relation to the recent revival of *Das Adam Smith Problem* from the perspective of moral philosophy. I will refer to these reinterpretations only selectively in as much as they allow me to further clarify those aspects that I believe are of a narrower economic concern in relation to the view of the self and his tendency to self-deceit.
another feels in her situation. That is, instead of just putting ourselves in another person’s place, we can imagine ourselves as another person.

As a founding pillar of Smith’s account, sympathy is first and foremost to be seen as a motivation to imagine oneself to be in a different position and circumstance, in other words to identify with others.18

Sympathy, as Fontaine contends, is furthermore an emotional act, implying that a person “feels into” (1997, 262) others’ feelings, thoughts and experiences (263). This idea is also proposed by Sugden (2002, 71-3), shedding light on the importance of affective states and how one person’s affective state influences another’s as constituents of sympathy. He emphasizes that participating in society via sympathy “is an urge… which gives pleasure to man.” He particularly brings in Smith’s theory in relation to what interacting agents feel, i.e. what agents experience when they act or are being acted upon.

Sympathy is to be seen as a principle in human nature, a disposition and not only a capacity (Montes 2003, 83). From this it follows that there is also a natural tendency to contribute to the imaginary exchange for its own sake, as Montes makes clear. Sympathy cannot be reduced to an act of choice (Sugden 2002).19 Contributing to the imaginary exchange is not a question of choice. And yet, sympathy is a motivation, as Montes (2002) contends when he brings in its broader circumstantial or situational sense.

Hence sympathy as it is used here does not denote any concordance of feelings or thoughts as the contemporary use of the term “to feel with” suggests (Fontaine 1997, 262).20 Feeling with others (which implies that one cares for the wellbeing of others) conveys a very strong sense of sympathy. This is the case when sympathy is equated with benevolence or altruism (Ashraf et al. 2005).21 When the present analysis advocates a weaker use of sympathy in terms of an imaginary exchange, this is not to deny that Smith considered “multidimensional and realistic human beings” (Ashraf et al. 2005, 142). The motivation of self-love when seen in this light is in no way a contradiction to sympathy. Sympathy only adds complexity to what, according to Smith, remains the dominant motivation, namely self-love. Also, for the problem we deal with here, we don’t need sympathy in the strong sense (of altruism). Sympathy as understood here does not denote any specific motivation. If the weak sense of sympathy also sees in it a motivation (as outlined above), then it simply denotes that in Smith’s view the individual participates in the imaginary exchange.

When sympathy in the strong sense is used, it is usually with a view to highlighting that in Smith’s view people were motivated not only by self-interest but also by their interest in...

18 Force (2003, 28-35) has written on sympathy and its link with identification.

19 Sympathy in this view is at the foundation of rational choice (theory), as Sugden (2002) also suggests. The idea I believe Smith had is to conceive of sympathy in terms of an emotion, and this is different from seeing in it a preference. One cannot have a preference for an emotional disposition and referring to sympathy exclusively along rationalistic lines would be misleading. As a consequence, sympathy (in the sense of exchanging places in the imagination) cannot be preferred or not, but is an essential characteristic of the self.

20 This is a logical consequence of the broader view of sympathy adopted here, which goes beyond seeing in it a foundation of man’s moral judgment (Raphael et al. 1984). It is in line with Haakonssen’s assertion quoted by Montes (2003) that sympathy is an “act of practical imagination … we cannot get to the stage of either approving or disapproving of a standpoint until we see it is a standpoint. Sympathy in the most important Smithian usage is this latter process which is preparatory to any assessment of people … it is not assessment itself … Smith often uses sympathy in both the traditional sense of approval and in the more original sense explained here” (85).

21 This use of the term has been rejected by many scholars of the history of economic thought (Brown 1997; Raphael et al. 1984), who contend that Smith’s concept of sympathy cannot be equated with specific motivations such as altruism or benevolence.
others. This is not contested, but the focus here is on another aspect in relation to self-love
that Smith was concerned with, namely self-deceit. The following quote by Bryson may be
read as a nice summary of the weak sense in which sympathy is used: “Sympathy … is … a
power of the imagination which allows a person to put himself in another’s place, to see the
world through that other man’s eyes, to feel its pressures and rebuffs through his sensitivities.
It is a fellow-feeling, but it is not pity nor compassion, which are feelings with another over
his sorrows and adversities; sympathy allows us to participate in any passion or experience of
another. It is the ability we have as human beings to receive communication … from and
about our fellows” (1968, 160).

We have seen that in Smith’s view of self-love as outlined above, the self is not at all times
sure about what he wants. Foolish ambitions regretted after the act are a case in point.
Fontaine (1997) has very much emphasized the idea that forceful identification is the
precondition for acquiring knowledge on the intention (and motivation) of others, which is
crucial in imperfect markets. I would add a further implication of empathic identification as a
consequence of Smith’s view of the self outlined above: one feels into others in order to get to
know not only their intentions but also one’s own. The idea is that knowledge of others is
crucial to acquiring knowledge about ourselves. In Smith’s view, without sympathy much of
our knowledge about others and about ourselves would be impossible. His reference to
society as a communicating mirror without which man could not “think of his own character”
(Smith [1759] 2001, 110) also reflects this idea.22

We have seen that self-deceit in Smith’s view is part of man’s nature. There is no essential
difference between Smith’s view on man in his economic and non-economic work in the first
place. Self-love is apparent all over and hence also self-deceit.23 However, despite his
extensive references to the “delusions” ([1759] 2001, 159) and “misrepresentations of self-
love” ([1759] 2001, 137;160), social order in his view does not solely depend on human
psychology. As he said, “self-deceit, this fatal weakness of mankind, is… the source of half
the disorders of human life” ([1759] 2001, 158). And note that it is half of the disorders, not
all of them.

In Smith’s view, the other half, I think, is to be attributed to bad institutions.24 While this
section has dealt with the foundations of individual self-deceit, the next sections will further
develop Smith’s argument on self-regulating social forces (section three) and how these are to
countervail self-deceit (section four). It is sympathy that enhances the individual’s
understanding of her limits, which are also the limits of self-love that exist in society.

3) Sympathy and the foundation of rules: the self-regulation of society

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22 If man is brought into society, his “desires and aversions, his joys and sorrows, will now often become the
causes of new desires and new aversions, new joys and new sorrows: they will now, therefore, interest him
deeply, and often call upon his most attentive consideration” (Smith [1759] 2001, 111).

23 It has been argued that Smith differentiated between various degrees of self-love in different spheres of
intimacy. According to this view, self-love prevails in markets (where we deal with strangers) and benevolence
in the family or the neighbourhood (Coase 1976, 27ff; Nieli 1986). Fontaine (1996) criticizes this schematization
because it neglects the empathic exchange in the imagination.

The idea that Smith meant self-love to prevail in The Wealth of Nations and benevolence in The Theory of Moral
Sentiments is related to the above schematization. One consequence of this view also is that Smith’s economic
analysis was separated from his non-economic analysis. Today this view of a rigorous separation between both
of his analyses and also between economic and non-economic phenomena in general is reconsidered.

24 I owe this thought to Eric Schliesser.
**The Theory of Moral Sentiments** can also be read as an account of the autonomy of the social self in which sympathy and man’s disposition to sympathize are at the centre stage. The strength of sympathy is that it works in both directions. It relies on the existence of at least two functions embodied in the actor and the spectator. When the actor puts herself into the circumstances and the position of another (i.e. the spectator), she knows at the same time that the other person will do the same (i.e. the spectator will also put himself into the circumstances and the position of the actor). From the imaginary exchange Smith derives important mechanisms of social control since it reinforces the actor’s tendency to consider the effect that her behaviour might have on others. At the foundation of this social mechanism is the motivation of social approval. A main feature of sympathy among humans, according to Smith, is that actors are permanently exposed to approval or disapproval of their behaviour. Society is seen as a system of mutual attention and attraction. In society, human values and behaviour are not neutral, but they are incessantly judged. This social approval/disapproval finds its origin in the omnipresence of spectators. And it works because – as a consequence of sympathy – human beings are not indifferent to these evaluations of others. As a result there is a tendency to moderate the expression of feelings that are not approved of by others or to adapt one’s behaviour to what others regard as proper in the specific situation. This is how rules of behaviour develop (Elsner 1989, 201ff; Levy and Peart 2004). What we have described here is the concept of self-regulation, which is at the heart of Smith’s account of social order.

Smith proffered a new account of society and its functioning in which social and moral norms also arise in the absence of religious authority or the state.

These general rules are formed bottom up, so to speak, and “ultimately founded upon experience of what, in particular instances, our moral faculties, our natural sense of merit and propriety, approve, or disapprove of. We do not originally approve or condemn particular actions; because, upon examination, they appear to be agreeable or inconsistent with a certain general rule. The general rule, on the contrary, is formed, by finding from experience, that all actions of a certain kind, or circumstances in a certain manner, are approved or disapproved of” (Smith [1759] 2001, 159). Smith insists that to “the man who first saw an inhuman murder, committed from avarice, envy, or unjust resentment, and upon one too that loved and trusted the murderer… complain more of the perfidy and ingratitude of his false friend, than of the violence which had been done to him, there could be no occasion, in order to conceive how horrible such an action was, that he should reflect, that one of the most sacred rules of conduct was what prohibited the taking away the life of an innocent person, that this was a plain violation of that rule, and consequently a very blamable action. His detestation of this crime, it is evident, would arise instantaneously and antecedent to his having formed to himself any such general rule” (159).

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25 In his account of Adam Smith, Macfie (1967, 70) correctly reminds us that Smith’s (philosophical) theory is also an implicit social theory, because it recognizes the autonomy of the social.

26 The concept of sympathy as a form of social control is also shared from a philosophical perspective by Forman-Barzillai (2005).

27 In their discussion of the other rational species problem, Levy and Peart (2004) bring in Smith’s concept of sympathy, in the sense of “trading for approbation”, which is creative of moral norms, i.e. generosity where standard approaches fail, namely in situations of inequality and in the absence of enforcement. Drawing on the classical prisoner’s dilemma, they show that katallactic rationality depends on sympathy, i.e. the actor knows that his choice will be judged by a future spectator and he will take into account the future approbation / disapprobation which follows from his choice (343).

28 “When these general rules, indeed, have been formed, when they are universally acknowledged and established, by the concurring sentiments of mankind, we frequently appeal to them as to the standards of judgment, in debating concerning the degree of praise or blame that is due to certain actions of a complicated
This is how sympathy accounts for the creation and pursuit of moral rules. In his account of self-regulation, the individual and his selfishness are bound by the social forces described above.

Although, Smith pursues, “it may be true, therefore, that every individual, in his own breast, naturally prefers himself to all mankind, yet he dares not look mankind in the face, and avow that he acts according to this principle. … In the race of wealth, and honours, and preferments, he may run as hard as he can, and strain every nerve and every muscle, in order to outstrip all his competitors. But if he should justle, or throw down any of them, the indulgence of the spectators is entirely at an end. It is a violation of fair play, which they cannot admit of. This man is to them, in every respect, as good as he: they do not enter into that self-love which he prefers himself so much to this other, and cannot go along with the motive from which he hurt him. They readily, therefore, sympathize with the natural resentment of the injured, and the offender becomes the object of their hatred and indignation” (79). This is how Smith’s sympathy first provides for the suppression of pure selfishness and the adherence to rules of fair play and honesty. Moral rules are important bounds to the excesses of self-love. Smith considers that the idea of self-regulation as he conceived it depends on these bounds.

Smith compares the relation between the individual and society with a looking glass (self). If man is brought into society, he is, writes Smith, “immediately provided with … [a] … mirror… [which] is placed in the countenance and behaviour of those he lives with” ([1759] 2001, 110). After what has been said on sympathy, this means that the social mirror does not only reflect man’s feelings, thoughts and experience but also judges them. Just as there are mirrors that amplify or suppress the original object, the social mirror amplifies or suppresses the original sensation by reflecting approval or disapproval. In this sense sympathy is related to what Smith was referring to as the strongest desire of all, namely the human desire to be attended to. This desire has often been referred to as a perfect example of human vanity but I believe it is particularly crucial if the additional facet of sympathy focused on in the present section is to work at all. Because if people were indifferent to other people’s judgement, and in turn were not interested in judging others, then indeed self-regulation of society as it is based on informal norms would not be possible.

and dubious nature.” These standards are then “commonly cited as the ultimate foundations of what is just and unjust in human conduct … and this circumstance seems to have misled several very eminent authors, to draw up their systems in such a manner, as if they had supposed that the original judgements of mankind with regard to right and wrong, were formed like the decisions of a court of judicatory, by considering first the general rule, and then, secondly, whether the particular action under consideration fell properly within its comprehension” (160).

29 “Honesty is the best policy” according to Smith ([1759] 2001, 63).

30 This is not to downplay the role of formal institutions such as the law in Smith’s account. Rosenberg (1960) makes the case for formal institutions in Adam Smith’s Wealth of Nations. Muller (1993) also draws on The Theory of Moral Sentiments and emphasizes both the significance of formal and informal institutions. The idea was to emphasize that a certain degree of autonomy exists, even in the absence of formal rules, when informal institutions suppress excessive self-love. Given the weight of informal rules Smith attributed to the self-regulation of society, it is worth noting that he gives reasons for the most part why individuals adhere to these rules (or how they contribute to their development by their persistent evaluation of each other’s behaviour). When he stressed morality, he did not explicitly discuss why selfish people (under specific conditions) might also violate these rules. Elsner (1989) also makes this point in his analysis of sympathy and the emergence of rules of behaviour when discussing open questions in Smith’s account of institutions.
Smith’s insights into self-regulation go beyond markets.\textsuperscript{31} The concept of self-regulation is also apparent in his moral and social systems. In addition to the discussion of sympathy in the previous section in which the emphasis was on individual knowledge (of herself and of others), self-regulation constitutes an important facet of sympathy when the emphasis is on social order. The focus on Smith’s non-economic work shows that for Smith the market is not the only system of regulating human behaviour. At the foundation of markets, informal institutions are important bounds to the excesses of self-love. Smith refers to the controlling function of sympathy in terms of the “man without” or the “man within”, depending on whether these rules are located at the interpersonal or the intrapersonal level.

The picture that Smith draws of sympathy is quite powerful. The idea that the deceiving self can be counterbalanced by the imposition of rules suggests that self-regulation is at work at both the interpersonal and the intrapersonal level. The present section has focused on Smith’s account of society and the role of informal institutions in general.

But Smith also credits informal institutions with guarding against what he may have considered to be man’s most important weakness, namely his tendency to self-deceive. His insights into the suppression of self-deceiving agents will therefore be the focus of the next section.

4) Suppression of self-deceiving agents

Smith’s assumption of “a man within” divides people into two and brings out their conflicting motivations. In Smith’s prose this sounds as follows: “I divide my self, as it were, into two persons; and that I, the examiner and judge, represent a different character from that other I, the person whose conduct is examined into and judged of. The first is the spectator, whose sentiments with regard to my own conduct I endeavour to enter into, by placing myself in his situation, and by considering how it would appear to me, when seen from that particular point of view. The second is the agent, the person whom I properly call myself, and of whose conduct, under the character of a spectator, I was endeavouring to form some opinion. The first is the judge; the second the person judged of” (Smith [1759] 2001, 113).

While the man without can be seen as the public spectator, “[t]he man within” as Smith calls the personal side to it, is “reason, principle, conscience, the inhabitant of the breast … the great judge and arbiter of our conduct” (Smith [1759] 2001, 137). Countervailing self-deceit resembles the mirroring procedure described above at an interpersonal level, except that at this point it operates intrapersonally. Inner personal regulation is successful if the man within imposes on excessive self-love – or, to put it another way, if self-love and its excesses can successfully be bound by personal rules. If not, the delusions of self-love prevail.

Smith understood the power of rules that are partly internalized by our conscience. Nature, he writes, has not left us “without a remedy … to the delusions of self-love. Our continual observations upon the conduct of others, insensibly lead us to form to ourselves certain general rules concerning what is fit and proper either to be done or to be avoided. Some of their actions shock all our natural sentiments. We hear every body about us express the like detestation against them. This still further confirms, and even exasperates our natural sense of their deformity. It satisfies us that we view them in the proper light, when we see other people view them in the same light. We resolve never to be guilty of the like, nor ever, upon any

\textsuperscript{31} It is interesting to observe that the controlling function of markets is assumed to operate along similar lines. The market has an inherent mechanism, so to speak, in that it punishes cheats by ruining their reputation. It therefore eliminates them in a self-regulatory way by forcing them into bankruptcy. Tullock ([1985]2003) claims that this sanctioning mechanism of markets, on which much contemporary game theory is also built and which Smith did not discuss explicitly, must have been familiar to Smith when he referred to the “discipline of continuous dealings”.

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account, to render ourselves in this manner the objects of universal disapprobation. We thus naturally lay down to ourselves a general rule, that all such actions are to be avoided, as tending to render us odious, contemptible, or punishable, the objects of all those sentiments for which we have the greatest dread and aversion. Other actions, on the contrary, call forth our approbation, and we hear every body around us express the same favourable opinion concerning them. Every body is eager to honour and reward them. They excite all those sentiments for which we have by nature the strongest desire; the love, the gratitude, the admiration of mankind. We become ambitious of performing the like; and thus naturally lay down to ourselves a rule of another kind, that every opportunity of acting in this manner is carefully to be sought after” (Smith [1759] 2001, 159).

Smith is convinced that “these general rules of conduct... fixed in our mind by habitual reflection, are of great use in correcting the misrepresentations of self-love concerning what is fit and proper to be done in our particular situation. The man of furious resentment, if he was to listen to the dictates of that passion, would perhaps regard the death of his enemy, as but a small compensation for the wrong, he imagines, he has received; which, however, may be no more than a very slight provocation. But his observation upon the conduct of others, have taught him how horrible all such sanguinary revenges appear. ... He has laid it down to himself as an inviolable rule, to abstain from them upon all occasions. This rule preserves its authority with him, and renders him incapable of being guilty of such violence. Yet the fury of his own temper may be such, that had this been the first time in which he considered such an action, he would undoubtedly have determined it to be quite just and proper, and what every impartial spectator would approve of.

But that reverence for the rule which past experience has impressed upon him, checks the impetuosity of his passion, and helps him to correct the too partial views which self-love might otherwise suggest, of what was proper to be done in his situation. If he should allow himself to be so far transported by passion as to violate this rule, yet, even in this case, he cannot throw off altogether the awe and respect with which he has been accustomed to regard it. At the very time of acting, at the moment in which passion mounts the highest, he hesitates and trembles at the thought of what he is about to do: he is secretly conscious to himself that he is breaking through those measures of conduct which, in all his cool hours, he had resolved never to infringe, which he had never seen infringed by others without the highest disapprobation, and of which the infringement, his own mind forebodes, must soon render him the object of the same disagreeable sentiments. ... [H]e is terrified at the thought of violating so sacred a rule, and at the same time is urged and goaded on by the fury of his desires to violate it. He changes his purpose every moment; sometimes he resolves to adhere to his principle, and not indulge a passion which may corrupt the remaining part of his life with the horrors of shame and repentance; and a momentary calm takes possession of breast, from the prospect of that security and tranquillity which he will enjoy when he thus determines not to expose himself to the hazard of a contrary conduct. But immediately the passion rouses anew, and with fresh fury drives him in to commit what he had the instant before resolved to abstain from. Wearied and distracted with those continual irresolution, he at length, from a sort of despair, makes the last fatal and irrecoverable step; but with that terror and amazement with which one flying from an enemy, throws himself over a precipice, where he is sure of meeting with more certain destruction than from any thing that pursues him from behind. Such are his sentiments even at the time of acting; though he is then, no doubt, less sensible of the impropriety of his own conduct than afterwards, when his passion being gratified and balled, he begins to view what he has done in the light in which others are apt to view it; and actually feels, what he had only foreseen imperfectly before, the strings of remorse and repentance begin to agitate and torment him” ([1759] 2001, 160-1).
What is important is that next to the suppression of dishonesty discussed in the previous section, Smith considered the suppression of self-deception by inner (or what we would today call ‘internalized’) rules. He introduced these informal institutions because he believed that they would suppress excessive self-love both in the form of ‘other-’ and self-deception.

The above focus on self-deceit exposes the fallibility of the man within and gives significance to rules of conduct. Smith’s discussion of self-deceit shows very well how corruptible the self is. Macfie’s insights into the degree of corruptibility of the self, which is representative of man’s tendency to self-deceive, have led him to emphasize the priority of sympathy in Smith’s account (1967, 97-100). The present claim regarding the originality of Smith’s insights into the regulating force of informal institutions confirms Macfie’s findings in this respect. When we study Smith’s account of self-deceit, an understanding of the system of mutual attraction and attention is crucial.

The view of countervailing informal institutions that suppress self-deceit fits into the picture of self-regulation – except that it is the man within instead of the man without who exerts the controlling function. These institutions gain their force through negative feedback mechanisms exerted by man’s conscience and applied by the self, which has internalized certain rules of what is fit and proper. As long as these mechanisms function and inner rules are imposed, the human tendency to self-deceive is suppressed. Because of inner rules of morality that are at issue in the above examples referred to by Smith, man will not pursue foolish ambitions. The man in the above example will temper his resentment because it is – from the point of view of his inner man’s position and circumstance – excessive. The informal institutional solution Smith offers to the problem of self-deceit lies in morality. According to Smith, these moral bounds are important countervailing forces to the pursuit of foolish ambitions.

And yet, informal institutions that suppress self-deceit are only one side of the coin. The other side is that informal institutions can also amplify self-deceiving agents. If an institution approves of foolish ambitions, we deal with a lack of countervailing forces and with positive feedback instead of negative feedback. The following section will draw on an example of prevailing self-deceit that Smith gives us in a clear economic context.

5) Amplification of self-deceiving agents

We have seen that informal institutions are important because they countervail man’s tendency to self-deceive. And yet, informal institutions that suppress self-deceit are only one side of the coin. The other side is that informal institutions can also amplify self-deceiving agents. If an institution approves of foolish ambitions, we deal with a lack of countervailing forces and with positive feedback instead of negative feedback. The following section will draw on an example of prevailing self-deceit that Smith gives us in a clear economic context.

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5) Amplification of self-deceiving agents

We have seen that informal institutions are important because they countervail man’s tendency to self-deceit. The problem is that, alternatively, they may also amplify this human penchant. And the parable of the poor man’s son, which, according to Smith, is significant with respect to self-deceit, also indicates its possible amplification in markets. In this parable, Smith refers to an economic motivation and presents self-deceit in a precise economic context. We will deal with it in terms of foolish ambitions and then emphasize the role of informal institutions.

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32 According to Coase (1976, 26) an adequate institutional structure is necessary for the economy to function and in particular it is the observance of moral codes that make possible the market system because they greatly reduce “the costs of doing business with others and must therefore facilitate market transactions” (28-9). It is not fully clear whether in his view the human tendency to self-deceive is to be held in check by informal institutions too. Coase recalls that in Smith’s view self-deceit is typically offset by social benefits (17) because the “the rest of us gain” (24), but does not explicitly answer how this is possible at all. My conjecture in the previous section was that Smith conceived of informal institutions as barriers to self-deceit. We are not, according to Smith “without a remedy... to the delusions of self-love” because we “form to ourselves certain general rules concerning what is fit and proper either to be done or to be avoided” ([1759] 2001, 159). The present section qualifies this countervailing function of informal institutions.
The poor man’s son sees a rich man in his carriage and aspires to all the riches, then spends his entire life obtaining them. The story is presented from the point of view of an old man who looks back at his career – after the act so to speak – and becomes aware of the foolishness of his ambitions.

“The poor man’s son, whom heaven in its anger has visited with ambition, when he begins to look around him, admires the condition of the rich. … He is displeased with being obliged to walk afoot, or to endure the fatigue of riding on horseback. He sees his superiors carried about in machines, and imagines that in one of these he could travel with less inconveniency. … He thinks if he had attained all these, he would sit still contentedly, and be quiet, enjoying himself in the thought of the happiness and tranquillity of his situation. He is enchanted with the distant idea of felicity. It appears in his fancy like the life of some superior rank of beings, and, in order to arrive at it, he devotes himself for ever to the pursuit of wealth and greatness … through the whole of his life he pursues the idea of a certain artificial and elegant repose which he may never arrive at, … if in the extremity of old age he should at last attain to it, … it is then, in the last dregs of life, his body wasted with toil and diseases, his mind galled and ruffled by the memory of a thousand injuries and disappointments … that he begins at last to find that wealth and greatness are mere trinkets of frivolous utility, no more adapted for procuring ease of body or tranquillity of mind, than the tweezer-cases of the lover of toys” (Smith [1759] 2001, 181).

The poor man’s self-deceit clearly has a number of faces. From a psychology and economics point of view it has been interpreted as an example of a forecasting error by the poor man’s son with regard to the consequences of his actions. The psychological focus on the parable holds that the riches don’t make the poor man’s son as happy as he had expected. The emphasis here is on incorrect judgements about the consequences of one’s action (Ashraf et al. 2005, 138-9). The poor man’s son (mistakenly) believes that riches will make him permanently happy. In this psychological interpretation, however, the specific ambitions of the poor man are given, the focus being on the error in decision with reference to the evaluation of the consequences of the action.

In an alternative interpretation of the parable, self-deceit is identified at the level of the ambitions themselves (Griswold 1999). In this view, the poor man’s son’s unhappiness is caused by a misunderstanding of what can in fact make people happy at all. With reference to the difference between contentment and tranquillity (which highlights the distinction between two states of happiness, the former relating to the frustration caused by man’s unlimited desires, while the latter builds on the extinction of these desires) Griswold claims that Smith represents the (stoic) tranquillity view of happiness. This view of “true” happiness is then the reference for “false” happiness caused by the liberation of our desires, and Smith’s parable of the poor man’s son is indicative of the general individual unhappiness that accompanies modern societies. For Griswold (1999) this individual unhappiness is the price that modernity has to pay for its economic development, which is built on the liberation of human desires.

My own interpretation builds on Smith’s view of the self outlined in section one above. It focuses on the imperfect knowledge of the self and his uncertainty with reference to what he wants and what he is. The poor man’s son in this view experiences a crisis of identity (or in other words, he looks at his own character from a different point of view). His value criteria change and from the point of view of this change, his previous ambitions disappear as an “illusion of the imagination” (Smith [1759] 2001, 115).

He sees himself as having pursued foolish ambitions, but not because his ambitions were frustrated: I believe that in the end his ambitions were less frustrated than the psychological or moral focus would suggest. First, because in reality he has become rich, so he has succeeded in realizing his ambitions. And second, because he never thought that riches would really
make him happier. When Smith tells us that the poor man’s son only wanted to “possess the means of happiness” (182), we are also supposed to know that he did not confuse the means with the end. He never believed that the pursuit of riches would make him happy in the first place. This is also why I believe he cannot be mistaken about the consequences of his decision. In this light, the parable is not primarily about a forecasting error. Through the lens of sympathy, the point Smith makes is not only that the poor man’s son aspires to riches because he (falsely) believes that these riches will make him (permanently) happier, nor does it deal solely with a cognitive error in the processing of information.

Also, in response to Griswold, I think that the focus on the stoic (or antique) vision of how people can achieve “true” happiness in the form of tranquillity that is believed to be rewarding in life and not to be achieved by the pursuit of riches conflicts with Smith’s modern reinterpretation of the pursuit of wealth as being at the same time at the foundation of moral improvement. This interpretation is also, I believe, shared by Griswold (1999, 217-7).

To my mind, the parable of the poor man’s son also makes clear that sympathy is not necessarily a moral motivation. Sympathy does not automatically impose moral bounds on human ambitions. Smith does not leave us in any doubt that the admiration of riches when we look at it in moral terms is a significant corruption of moral sentiments. But instead of condemning man’s admiration of “the condition of the rich and the great” and his corresponding disdain for the man in poor condition, he seeks to explain it. Self-deceit remains a part of human nature after all. For Smith, the motivation to become rich is (properly) to be liberated from any moral bounds. He removes the moral aspect from the pursuit of riches in this way and displaces the moral discourse of Aristotle, as also noted by Diatkine (2000, 501). The basic rationale here, I believe, is that in view of economic growth the human imagination with regard to material progress has no need to be down-tuned by countervailing forces (as may seem necessary in times of economic stagnation and decline). The ensuing liberation of individual desires particularly in the economic context also constitutes one of Smith’s conceptual innovations.

The explanation of self-deceit in terms of cognitive error (Ashraf et al. 2005) or moral corruption (Griswold 1999) thus only represents one side of the coin. I have argued that there is also an existential orientation in Smith’s parable.

Be that as it may, what has become clear is that an adequate interpretation of the specific nature of self-deceit in the parable still remains open. However, it is beyond dispute that the parable is about an agent who has fooled himself. All interpretations given above have in common that the poor man’s son has not been fooled by an outside authority, be it religious or

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33 As Smith says, the poor man’s son does not “imagine[s] that... [the rich]... are really happier than other people: but he imagines that they possess more means of happiness” (Smith [1759] 2001, 182).

34 Even so, it is important for the account adopted here to draw attention to the fact that Smith – unlike Bishop Butler, who wrote about self-deceit in his time – confines himself to condemning human nature (or vices related to it). Self-deceit was seen as natural, and although it distorted man’s judgement and rendered many of his aspirations foolish, it was not seen as a wrong in itself. This was also a conceptual innovation compared with the discourses on self-deception common at his time. Bishop Butler’s view typically reflects this “old” view of self-deception as an ultimate moral failing, according to which wrongdoing stems from an over-regard or partiality. In self-deception, this partiality leads to wrong moral judgements. Self-deception is condemned because it hinders men in their quest for virtue and because it corrupts man’s conscience. Self-deceit, then, “is therefore so far from extenuating guilt, that it is itself the greatest of all guilt in proportion to the degree it prevails; for it is a corruption of the whole moral character in its principle” (Butler [1726] 1995, 178-9). This is also how Smith removed morality from the discourse on self-deceit in relation to economic motivation by introducing a new – economic – focus on problems that were dealt with hitherto primarily from a non-economic point of view. It was in fact Smith’s innovative view of human action (and its non-intentional consequences) that led him to overcome the view of self-deception in the economic context.
secular. It is not so important to conclude on the exact nature of the deceit; what is important for my analysis is that in the parable self-deceit is amplified, and to this we now turn.

After what has been said, Smith’s account of sympathy and his understanding of society as a system of mutual attention and attraction emphasize again the importance of informal institutions. The poor man’s pursuit of wealth is amplified by the approval of others. As we have seen, according to Smith, if we live in society we cannot escape from the regard of others. Between the rich and the poor man an imaginary third person, the spectator, intervenes. Consequently, the poor man thinks what the rich man thinks what the spectator thinks. The poor man does not only admire the rich man because he thinks that riches are admirable as such, but also because riches are admired by others. Hence, his admiration of riches much depends on what is admired by others.

In terms of sympathy, the poor man’s son’s self-deceit is amplified by a social norm. And seen in this light, the imaginary exchange can actually also reinforce the illusions of the imagination. Living “in society”, Smith adds, “there [indeed] can be no comparison, because in this, as in all other cases, we constantly pay more regard to the sentiments of the spectator, than to those of the person principally concerned, and consider rather how his situation will appear to other people, than how it will appear to himself” (Smith [1759] 2001, 182).

In Smith’s view the parable is on norms in association with riches. Riches, according to Smith, are the natural objects of admiration.35

It is difficult to imagine how the poor man’s son’s illusion is to be corrected, if it should be at all. Adam Smith obviously seemed to believe that it should not, since a correction of this human ‘irrationality’ (by alternative norms, for example) would hinder economic activity. In this sense, Smith considered self-deceit as “functional” (Gerschlager 2005); it “rouses and keeps in continual motion the industry of mankind” (183).

Thus, the parable also implicitly suggests that the poor man’s son cannot get rid of his foolish ambitions. The poor man’s son in the parable becomes aware of the trick that self-love has played on him only in a splenetic moment (and after the action). Smith understands that to “the languor of disease and the weariness of old age, the pleasures of the vain and empty distinctions of greatness disappear. To one, in this situation, they are no longer capable of recommending those toilsome pursuits in which they had formerly engaged him. In his heart he curses ambition, and vainly regrets the ease and the indolence of youth, pleasures which are fled for ever, and which he has foolishly sacrificed for what, when he has got it, can afford him no real satisfaction. In this miserable aspect does greatness appear to every man when reduced either by spleen or disease to observe with attention his own situation, and to consider what it is that is really wanting to his happiness” (183). The parable suggests that the poor man’s son’s awareness won’t remain, because either both his health will be restored and self-deceit re-imposed, or he will die.

The concern that Smith perhaps had in mind here is that without foolishness, economic activity would not take place at all, and those times of “pain and sorrow” would consequently (have to) prevail in which “[o]ur imagination seems to be confined and cooped up within our own persons” (183).

35 Because wealth, power and success are the “natural objects” (62) of admiration, Smith argued, in fact, that people cannot help aspiring to them. Man has a “disposition to admire, and almost to worship, the rich and the powerful, and to despise, or, at least, to neglect persons of poor and mean condition” (Smith [1759] 2001, 61). What is true for wealth and power is equally true for success. Admiration of success in public life is founded on the same principle as our respect for wealth and greatness.
We have seen that sympathy also exerts positive feedback and with reference to Smith’s parable this explains why informal norms do not always countervail self-deceiving agents, as was the case with morality in the previous section, but also amplify them.

6) Conclusion

The fact that the founding father has not bequeathed us with his explicit position on the exact articulation between his two major books does not repudiate the resumption of Das Adam Smith Problem referred to in the introduction. It should have become clear that it was not my intention in the present paper to tackle this problem and the important questions that lurk behind it.

The present analysis instead has selected one aspect in his non-economic work, the economic relevance of which Adam Smith was unambiguously explicit about, namely the human tendency to self-deceive. The present analysis of this human tendency has also revealed that economic and non-economic phenomena are not strictly separated.

Smith’s account of self-deceit is deeply rooted in his view of the self, which he saw as incomplete and dependent on others. This view is difficult to reconcile with the claim for the self with which he is regularly associated, also implicit in the self-interest assumption, namely that he always knows best what he wants. Smith’s individuals live in a world of self-delusion and Smith, in contrast to most modern economists, was importantly concerned with this fact.

A limitation of the present analysis is that it does not discuss whether Adam Smith’s account of self-deceit at the individual level can be accommodated by rational choice theory (in terms of a violation of some axioms or of self-interest for example). The present paper has chosen to follow Smith’s account and draw on self-deceit against the background of a broader interpretation of rationality (including a reflection of one’s ambitions).

At the same time, Smith is prominently attributed with being an advocate of the market view. In the typical market view as outlined in the introduction, self-deceiving agents are to be countervailed by market forces. The present paper has revealed that in Smith’s view markets are insufficient to countervail self-deceit. In fact, according to the present analysis the originality of Smith’s account of self-deceit lies in his insights into informal institutions as self-regulating social forces.

That informal institutions are crucial to countervail market failures is a general point that has first explicitly been made by Arrow (1971). In this view these norms of social behaviour including moral codes are society’s reactions to the limits of countervailing market forces (22).

Alternatively, informal institutions need not automatically support the economy. They can also amplify the human tendency to self-deceive and it is significant that in Smith’s parable referred to above, the poor man’s son’s illusion is not countervailed. The interpretation that I suggest for this is that Adam Smith might have overestimated society and its countervailing forces. For in the absence (or deficiency) of countervailing forces, man’s illusions indeed thrive and prosper in markets.

End
Additional perspectives

Let me recall that I started with Adam Smith’s claim that self-deceit was a function of economic development. In fact, Smith went one step further, claiming that self-deceiving agents should be regarded as “well”36 for economic activity ([1759] 2001, 183).

After all, was Smith correct to believe that the economy depends on illusions? I think that his concern for human nature (“as it is”) merits more economic attention than has usually been devoted to it. If Smith is correct and illusions are a driving force behind economic growth, further research is needed to obtain a clearer picture. How much of economic growth actually depends on this trait?

In this sense, Smith’s assertion about the (positive) economic implications of self-deceit is also indicative of his insights into illusion and the foolishness of motivations and beliefs that can motivate economic activity. From an economic point of view, though, recognizing self-deceit as a motivating force is not the same as approving of its efficiency.

It is true that Smith’s foolish ambitions (and beliefs about the world) can indeed motivate people to work, save and invest as the poor man’s son in the parable obviously did. In economic terms, however, the consequences need not necessarily be ’good’.

Smith’s belief ignores the fact that if ambitions are distorted, resources are also wasted because efforts are invested on the basis of incorrect information. If people engage in the pursuit of foolish goals (similar to sticking to their false beliefs about the world), they will not be able to engage in alternative and less foolish ones and this will typically result in misallocation of economic resources.

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36 According to Smith “it is well that nature imposes upon us in this manner” (183).
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