

## 2. A Methodological Appraisal of Schmoller's Research Program

### I. Historical and Ethical Approach

Speaking on the occasion of his inauguration as rector of the University of Berlin in 1897, Gustav von Schmoller (1838–1917) remarked proudly: “Today’s economics has reached a historical and ethical conception of nation and society contrary to rationalism and materialism” (Schmoller 1897, 26). He affixed the label “historico-ethical” to his German Historical School (Schumpeter 1954b, 812). Although both historical and ethical factors have been expelled from the scope of mainstream economics, there always has been some sort of yearning for those factors behind the seeming scientific objectivity of economics. In this article I analyze the structure of the historical-ethical approach in Schmoller’s economics in order to derive its relevance in modern times.

As Joseph Alois Schumpeter related, economics grew from two distinct roots: the philosophical speculation of *Weltanschauung* and the discussion of current practical affairs, or, briefly, “philosophy” and “policy” (Schumpeter [1914], 21; 1954a, 9–11). By the first root Schumpeter meant the philosophers’ ideas on society that originated with Aristotle and were brought to completion as “moral philosophy”; by the second he meant “popular economics,” which was molded by merchants and officers in their ordinary business life and coined mercantilism and cameralism, respectively.

Although economic thought had been brought up initially by “philosophy” and “policy,” it was established later as a science by getting rid of them. Thus economics refrained once and for all from indulging in the speculation of *Weltanschauung* without observations of reality, on the one hand, and from recommending practical policy without recognition of the interrelationship among individual economic affairs, on the other. Specifically, economic science was established by growing attempts in seventeenth- and eighteenth-century Europe to discover the mechanism of economic phenomena on the basis of empirical facts. Thus British classical economists first found in the emerging capitalist economy an orderly mechanism with regard to the formation of prices and income. As the two sources of economics, we can say, philosophy stimulated ethical inquiries into a microeconomic order through the topics of justice in exchange, virtue in trade, legitimacy of interest and so on, and policy provided the task of finding a macroeconomic order through the topics of money, prices, balance of trade, and the like. Classical economics, in this way, jettisoned ethical and political elements to bring into relief an economic mechanism with regard to both micro and macro aspects.

The fact that a scientific system of economics was established and the scope and methods were defined for its system means that the conception of economy as the object of study was fixed in a certain way. Establishment of a scientific system is usually followed by development and elaboration within that system, on the one hand, and by criticism and controversy from outside the system, on the other. Neoclassical economics and Marxism were examples of the internal development and elaboration of classical economics, and the German historicism was a case of external criticism and controversy.

The German Historical School advocated a historical perspective that had never played a paradigmatic role in economic thinking, and it claimed that the economy can be properly conceptualized only from that perspective. For its proponents, the historical approach was a challenge to the theoretical approach of classical economics. Their emphasis on historical research was based on a new conception of economics, a policy-oriented economics: they were politically opposed to both *laissez-faire* economics and Marxian economics. For them, Schumpeter's notion of the two sources of economics, i.e., philosophy and policy, should not be jettisoned as being of no more use; rather, it should be made full use of as the basis for a new direction of economics.

It was believed that philosophy and policy, if placed in a historical perspective, could positively contribute to the formation of a different type of economics, because both moral values and political programs were now the objects of empirical and objective historical studies. It is important to realize that in the mind of the German Historical School, philosophy and policy were combined from a historical viewpoint. The new economics of the German Historical School, paradigmatically opposed to classical theoretical economics, did not simply consist in the devotion to an immense amount of historical facts. It claimed the two prescientific levers, i.e., philosophy and policy, as the guiding stars for historical research. Thus Friedrich List anticipated the fundamental approach of the German Historical School: "Political economy is based on *philosophy, policy, and history*.... History mediates between two-sided inquiries of philosophy and policy" (List [1844] 1930, 41).

The German Historical School generally emphasized the importance of historical research in reconstructing economics, but it was Gustav von Schmoller, the leader of the younger German Historical School and of the *Verein für Sozialpolitik*, who explicitly combined ethics and history. For Schmoller, ethics gave meaning and direction to historical research in economics. Ethics, the knowledge of a guide for action, must not only be based on a general, abstract principle of moral philosophy, but it must also be applicable to individual, concrete cases of social policy for designing institutions or organizations. In other words, ethics integrated the two separate roots of economics, i.e., philosophy and policy, and the integration was attempted from a historical perspective.

Schmoller maintained that the basic condition of human culture, of which economy is a part, is a religious and moral system and that economic life cannot be understood without the knowledge of the historical development of

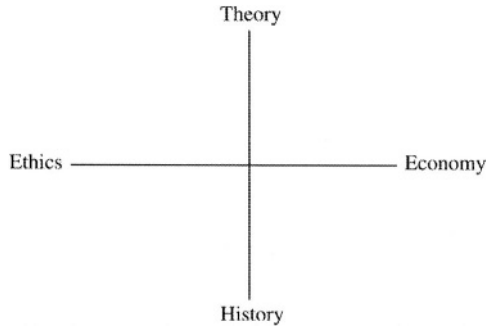
three norms: customs, laws, and morals. Economic institutions or organizations are not only natural and technical but also psychological and ethical in the sense that the social framework does not work without a consensus of ethical values even if that were technically feasible. In fact, the norms constitute the institutional framework of a society (Schmoller 1900, vol. 1, 1–75).

In discussing the past development of moral philosophy as a source of economics, Schmoller found in the speculative endeavors of *Weltanschauung* not so much visions leading to the discovery of an economic mechanism by the British classical economists, as morals leading to the foundation of social institutions in which the economic mechanism was found to function. In discussing another source of economics, namely the development of thought on practical problems in mercantilism and cameralism, Schmoller favored these practical doctrines rather than the abstract theories of their successors, namely the British classical economists, because the former depended on real experience. In other words, he found a framework policy for nation-building more important than macro- and microeconomic relations within a given framework. It should be emphasized that he expended the utmost effort to clarify practical policy in history rather than the doctrines of contemporary statesmen and scholars. Schmoller took both philosophy and policy seriously as the sources of a newly emerging historical economics by combining them under ethical as well as historical perspectives, and focused the aim of historical economics on the development of an institutional framework that conditioned the macro- and microeconomic mechanism. In this sense, the specification of Schmoller's work as "historical-ethical" indicates his unique position in the history of economics.

It is this combination of historical and ethical in Schmoller's approach that Friedrich Meinecke innocently called "an ingenious compromise between German idealism, its ethics, in particular, and positivism and empiricism in Western Europe" (Meinecke 1933, 148–49). The weight of the challenge of Schmoller's historical-ethical approach is illustrated by two controversies created by two aspects of that approach: the *Methodenstreit* between Schmoller and Carl Menger and the *Werturteilstreit* between Schmoller and Max Weber. Schmoller was criticized doubly for banishing theory because of extreme concern about historical research and ethical evaluation. If Schmoller had simply lost these two disputes, most of his essentials would have been denied. In fact, although these disputes appeared to be settled temporarily, the issues that manifested themselves in these debates are perennial. Here lies a reason why Schmoller's approach is now being reconsidered after fifty years of complete neglect.<sup>1</sup>

But the pretension of scientific objectivity by the use of historical research for the purpose of concealing an ideological standpoint is no longer maintained, even if it had some practical effects on Prussian civil servants. What is the real ingenuity in the historical-ethical approach of Schmoller? In the following sections I divide the history-ethics relationship into a methodological relationship between theory and history, on the one hand,

Figure 1. Analysis of Historical-Ethical Approach



and a substantive relationship between ethics and economy, on the other. In other words, I assume the vertical theory-history axis and the horizontal ethics-economics axis to visualize a broad perspective of the historical-ethical approach, as indicated in Figure 1.

## II. Theory and History

The *Methodenstreit* between Schmoller and Menger with regard to the relative importance of the theoretical method and the historical method in economics ended without a resolution. The antagonism between them is typically shown by their following exchanges of abuses: according to Schmoller, Menger only knew and confined himself to “a corner of the large house of our science” and took it for “the whole house” or “the best and fanciest salon in the house” (Schmoller 1888a, 293–94). In response, Menger asserted: “Schmoller’s view is compared to that of a navvy who wants to be regarded as an architect because he carried some stones and sand to the construction site” (Menger 1884, 46). Each of them relegated the other to such a lowly place in the total body of economics that they could not arrive at a reconciliation.

Most current economists would agree with Schumpeter’s appraisal of the *Methodenstreit*. In his *History of Economic Analysis*, he wrote: “In spite of some contributions toward clarification of logical backgrounds, the history of this literature is substantially a history of wasted energies, which could have been put to better use” (Schumpeter 1954b, 814). This rather negative assessment seems to include different reasons why the debate was a history of wasted energies. Schumpeter himself gave two different reasons on different occasions.

First, in his first book *Das Wesen und der Hauptinhalt der theoretischen Nationalökonomie* (1908), Schumpeter insisted that because historical and theoretical methods are concerned with different problems, different interests, different categories of hypotheses, and different goals, it is useless to quarrel about the relative importance of the methods. Confronted with the danger of

economics especially in the German-speaking world, he strongly advocated the separation and differentiation of history and theory on the ground of instrumentalist methodology (Shionoya 1990). According to instrumentalism, theories are not descriptions but instruments for deriving useful results; they are neither true nor false. From this methodological standpoint, a specific method can only claim usefulness for the treatment of a specific problem. Although instrumentalism guarantees the peaceful coexistence of history and theory, Schumpeter in *Wesen* tried to clarify the epistemological foundation of theoretical economics in support of Menger. Theoretical economics was defined as a static theory of exchange, and dynamic problems such as capital formation, credit, interest, profit, and crisis, together with all the problems of political, social, and cultural development were relegated to descriptive historical research. The proposal to suspend hostilities in the *Methodenstreit* was a practical expedient and agreed with the circumstances in which instrumentalism was originally devised as an arbiter of unsettled controversies in the natural sciences.

Second, after the publication of *Theorie der wirtschaftlichen Entwicklung* (1912) Schumpeter turned to a discussion of the cooperation of history and theory in order to deal with the dynamic problems of economy. In this case, the controversy between history and theory is useless for a different reason. Both inductive and deductive methods, or empirical and abstract methods, are required for what might be called a joint research between theory and history. In his 1926 essay on Schmoller, Schumpeter called the joint research *economic sociology* and interpreted Schmoller's research program as an approach to this discipline (Schumpeter 1926).

It does not make sense to argue in general terms, as has often been done in assessments of the *Methodenstreit*, that inductive and deductive methods, or empirical and abstract methods do not contradict each other but should cooperate with each other and that for this reason the dispute between these methods is meaningless. This argument does not resolve the *Methodenstreit*. As a matter of fact, the cooperation could not be expected either in Schmoller's field of detailed historical studies or in Menger's field of abstract theoretical studies. The *Methodenstreit* was a misnomer; the real issue was over the scope of economic science. The difference in method only reflected the difference in the scope of the subject matter. Historical science dealing with the concrete individuality of socioeconomic phenomena at large and theoretical science dealing with general concepts for limited, isolated economic phenomena demand completely different methods. It is crucial to find a field where cooperation between history and theory is necessary and feasible. Schumpeter characterized economic sociology as "a special field which, owing to the nature of its object, is not only a detailed and material-collecting discipline but also a theoretical discipline" (Schumpeter 1926, 369–70). He held that the subject matter of this discipline was institutions generally and social classes and business cycles in particular.

But Schumpeter did not accept Schmoller's research program as it stood. He demanded rather radical changes in its scope, methods, and methodology in

order to develop its strengths and limit its weaknesses. It will be illuminating to examine Schmoller through the looking glass of Schumpeter's view of economic sociology, which Schumpeter locates in the toolbox of economic analysis together with theory, history, and statistics (Schumpeter 1954b, 12). Discussed next are (1) the formal aspect, (2) the substantive aspect, and (3) the methodology of Schmoller's research program.

### 1. The formal aspect

The formal aspect of the research program of Schmoller's economics consists of three steps: (i) the observation and description of economic phenomena according to time and space, (ii) the definition and classification of the phenomena by a coordinated system, and (iii) the causal explanation of the phenomena and recognition of their interrelations (Schmoller 1900, vol. 1, 12; also Schmoller 1911, 455). This program indicates an apparently endless scenario of empirical research. Although Schmoller does not exclude from economics the natural scientific method, general concepts, and regularity, his own research program is confined to the collection and summarization of historical data; he emphasizes the importance of accumulating monographs on historical studies. This was rooted in his basic recognition that economics must deal with complicated and various phenomena and that it is not sufficiently advanced to allow the use of deductive-abstract methods and the formulation of laws. The claim of the German Historical School is not the denial of theory in general but the need for more empirical studies before the theoretical formulation of wide and complicated phenomena in the historical perspective can be undertaken productively.

Comparing empiricism with rationalism, Schmoller held that the development of human recognition takes place as the alternation of empirical and rational methods; he insisted that instead of making a rash generalization on a poor empirical basis, one should engage in empirical research before beginning the theoretical treatment of historical materials (Schmoller 1888b, 147–50). His principle was: “When laws don't exist, we must be content with the broad observation of reality, the classification of these materials, and the inquiry of causes” (Schmoller 1888a, 283–84). These three tasks are nothing more than the three steps described above as the formal aspect of Schmoller's research program; thus, what is meant by the causal explanation in the third step is not based on theories deduced from assumptions but on ad hoc conjectures.

Schmoller's *Grundriss der allgemeinen Volkswirtschaftslehre* (2 vols, 1900–04) was an attempt to develop a theoretical system of economics on the basis of historical knowledge, and economists were surprised to see that he undertook a theoretical work so soon. Although its theoretical content is meager, the book indicates that the German Historical School does not deny theoretical formulation.

## 2. The substantive aspect

It is the substantive aspect of Schmoller's research program that determines the content of the program. This aspect relates to a set of specific visions and preconceptions, as a presupposition of empirical research, on how to perceive the subject matter. In his early work on the history of economic doctrines and methods Schumpeter summarized six basic viewpoints of German Historical School: (1) a belief in the unity of social life and the inseparable relationship among its component elements, (2) a concern for development, (3) an organic and holistic view of society, (4) a recognition of the plurality of human motives, (5) an interest in concrete, individual relations rather than the general nature of events, and (6) historical relativity (Schumpeter 1914, 110–13; 1954a, 176–80). We can hope for no better analysis of the methodological characteristics of the Historical School than this. Of these viewpoints, Schumpeter gave unqualified approval to (1) and (2); he agreed with (3) and (4) at least in their more moderate forms; and he abandoned (5) and (6) because they rejected *a priori* the possibility of a general and universal viewpoint.

The greatest significance of the historical method for Schumpeter was the recognition that historical materials reflect the development phenomenon, indicate the relationship between economic and noneconomic facts, and thus suggest how the disciplines of social sciences should interact. This recognition of the development and unity of social life is the combination of viewpoints (1) and (2), the essence of the German Historical School as Schumpeter understood it. For this reason Schumpeter found in Schmoller's research program the "outlook of a universal social science" (Schumpeter 1926, 365). It is well known that Schumpeter admired Marx, but he admired Schmoller for the same reason. He highly praised those scholars who had a grand research program covering the historical development and intertwinement of social aspects as a whole. Marx was one of them; another was Schmoller. Schumpeter offered the name "unitary Social Science" to Marx's vision of social evolution in the same sense in which he called Schmoller's program a "universal social science" (Schumpeter 1954b, 441). But Schumpeter noticed an important difference between Marx and Schmoller. He was critical of Marx's economic interpretation of history. He lumped together attempts at reducing a whole historical process to the action of one or two factors as a simple hypothesis of the "Comte-Buckle-Marx kind" and contrasted them with Schmoller's pluralist approach to which he was quite sympathetic (Schumpeter 1954b, 811).

While viewpoints (1) and (2) of the German Historical School relate to the scope of subject matter, (3), (4), (5), and (6) concern their methods. Schumpeter recognized a purely scientific value in the claims of (3) and (4), which are distinct from the assumptions of neoclassical economics, those of methodological individualism and of utility maximization. As to (3), i.e., the organic and holistic view of society, Schumpeter denied the alleged contention of the Historical School that a national economy has its own aims and

interests and thus cannot be split into an agglomeration of independent individuals, the view basically influenced by the philosophy of value in German historicism. Instead, he considered more acceptable the belief that individuals do not live in a vacuum but are conditioned by the institutional and cultural factors of a society. He interpreted Schmoller's view as follows:

the individual economies, which together comprise the national economy, stand in intimate mutual relations with each other. These relations are far more important than the ones which economic theory describes and which influence the individual member of the economy. They enforce in fact upon the individual a behaviour which is of a different kind and which must be explained in a way which is quite different from the one of which economic theory speaks ([1914] 1954a, 180).

This viewpoint is related to (4), i.e., the recognition of the plural motives of individuals. Rejecting the assumption of maximizing behavior of autonomous individuals, Schmoller emphasized that customs, laws, and morals constitute the institutional framework of a society and that the behavior of individuals is partly formed by institutions.

Referring to viewpoints (3) and (4), Schumpeter described the direction of research in the German Historical School that was labeled "historico-ethical": "the school professed to study *all* the facets of an economic phenomenon; hence *all* the facets of economic behavior and not merely the economic logic of it; hence the *whole* of human motivations as historically displayed, the specifically economic ones not more than the rest for which the term 'ethical' was made to serve, presumably because it seems to stress hyperindividual components" (Schumpeter 1954b, 812). It is viewpoints (3) and (4) that the old institutional economics after the Historical School emphasized, whereas the new institutional economics based on neoclassical economics denies them.

Schumpeter did not show much interest in viewpoint (5), i.e., the issue of individuality versus generality, and (6), i.e., the issue of relativity versus universality of social knowledge. Although the position of historicism used to be bound up with an interest in individuality and relativity, Schumpeter argued, historical interest should not prevent the possibility of general and universal knowledge. He found that (5) and (6) were not fruitful issues; thus he was critical of neo-Kantian philosophy, which, he said, went too far into these issues. Surprisingly, he found that Schmoller stuck to neither the individuality nor the relativity of historical phenomena:

he recognized ... how essentially similar the causal nexus in social science and natural science is; he also described the explanation of social phenomena in the form of cause and effect and in the form of laws ... as the aim of scientific effort. Indeed we find even the far-reaching proposition that all perfect science is "deductive." ... This proposition implies the acknowledgment that such a state of the science is possible in principle—even if in actual fact it should remain unattainable for us. It also



implies a complete rejection of the specifically historical belief in the "incalculable" and essentially "irrational" nature of social events. Schmoller goes further here than most of the theorists would have been prepared to do ([1914] 1954a, 170–71).

A different methodology for bridging the gap between theory and history was required. Max Weber's methodological work, consisting of the concepts of "understanding" (*Verstehen*) and of "ideal types," was a solution to the problems concerning viewpoints (3), (4), (5), and (6) (Shionoya 1992).

### 3. The methodology

Economic sociology, in Schumpeter's view, belongs to a category of theory and is subject to the instrumentalist methodology (Shionoya 1991). This methodological standpoint will serve as a test for Schmoller's research program. According to Schmoller, a theory or law must be nothing more than a summary or generalization of empirical facts. Since it is extremely difficult to grasp the complexity of the total historical developments of economic life, he insisted, we have not yet acquired what can be called a law or a theory. Schmoller's notion of theory involves a requirement that a theory should start from realistic assumptions that ought to be derived from an extensive observation of reality. It follows that this procedure would be valid only for a complete science as an ideal. He always maintained that "all progress of induction brings us deductively useful propositions and the most completed science is generally deductive" (Schmoller 1911, 478). In Schmoller's long-run view, by the continuous efforts of detailed empirical research and comprehensive summary, economists will approach an indisputable truth that is accepted by all" (Schmoller 1897, 9–10).

Instrumentalism, in contrast, asserts that assumptions or hypotheses are arbitrary creations of the human mind and need not be justified by facts, and that theories deduced from assumptions are not descriptive statements in themselves but instruments for understanding and explaining facts. Therefore, a theory is neither true nor false; it proves useful if it can cover an increasing amount of facts. Instrumentalism facilitates deductive attempts even when a sufficient amount of empirical data for a given area of study has not been collected according to the Schmollerian standard. Theory is not only a convenient device for summarizing, systematizing, and deducing a given body of observable facts but also a guide for exploring and predicting unknown facts. Whereas Schumpeter's instrumentalist methodology provided a prescription for the suspension of hostilities between history and theory when it was applied to the *Methodenstreit*, it could advise cooperation between history and theory when applied to Schmoller's research program. One does not need to engage in the never-ending process of data collection in order to develop realistic assumptions; instead, one should have a feedback process between theory construction and fact-finding in order to achieve a "unified

sociology or social science as the mentally ('theoretically') constructed universal history" (Schumpeter 1926, 382).

Schmoller remained a naïve empiricist; he did not have a coherent methodological approach. When he considered the nature of concept formation, he argued, while admitting nominalism instead of realism, that concepts were means for constructing thought, not perfect copies of reality (Schmoller 1911, 467–68). Since abstraction meant to him a deviation from reality, it was natural that he could not give a realist status to concepts. From this position it was only a step to instrumentalism. But he was so much absorbed in the classification of particulars into universal categories that he emphasized only in the negative vein that concepts cannot describe real individuality and therefore fundamental truth. As a result, he was only concerned with broad data collection so as to load concepts with rich content. His conception of a developed, ideal science seems to have been such that concepts and definitions already contained enough truth to deduce more important results. He could not proceed to the instrumentalist methodology from the nominalist notion of concepts and allow an instrumentalist role of assumptions and hypotheses as deliberate mental constructs, because in spite of his nominalist position his ultimate goal was scientific realism.

### III. Ethics and Economy

The second leading idea in Schmoller's economics is ethics. The place of ethical value judgment was definitely denied by Weber's thesis of value freedom. But the thesis that science should not deal with any ethical judgment does not deny Schmoller's ethical approach. Indeed, Schmoller was motivated by the social problems of Germany and concerned with the planning of social reform, but his social and political ideals can be separated from the formal structure of his approach. His treatment of ethical factors in economics was sufficiently careful to support the total structure of his thought, and I am concerned here with the formal structure of his ethical approach. It is a mistake to reject Schmoller's approach by the stereotyped notion of a value-free science.

Schmoller's view of economic institutions or organizations was that they are not only natural and technical but also spiritual and ethical. Insofar as economic phenomena such as price formation and income distribution are concerned, as is the case for British classical economists, it is not necessary to deal with the social framework in which the economic phenomena take place. In contrast, Schmoller believed that the historical evolution of institutions should be the theme of economics and focused on customs, laws, and morals as the social determinants of institutions. He described the intention of his *Grundriss der allgemeinen Volkswirtschaftslehre* as follows: "Economic behavior and economic institutions should not be derived only from value phenomena or something like instinct but, following the unity of today's human sciences, from psychological power in general, from sentiment and

instinct, from ethical ideas, and economic behavior should be grasped in the framework of morals, custom, and law” (Schmoller 1911, 448). As noted above, ethics gave meaning and direction to historical research in Schmoller's economics. According to him, in order to discuss economic institutions in a historical perspective, one must focus on the morals, customs, and laws that are embodied as facts in institutions. Three features are most significant with regard to Schmoller's ethical approach.

First, by morals Schmoller did not mean his own subjective moral judgments but objective moral judgments in the sense of historical facts. It is true that ethical and political ideals simply derived from metaphysical and nonempirical ground cannot be supported scientifically. In contrast, for Schmoller, ethical values were empirical materials in the historical research of institutional change. His ethical approach, it should be stressed, was not an attempt to mix values with facts, as he was accused, but that of dealing with factual values. He argued: “As ethics becomes more and more empirical so that it describes ethical duty, virtue, and good in the form of historical development rather than teaches norms, the elements of beliefs and their function in ethics naturally decline. Thus ethics gets near to social science or state science or what one calls today sociology” (Schmoller 1911, 438).

Second, in dealing with factual value judgments, Schmoller was opposed to the partial values advocated by political parties and social classes; he wanted to discuss universally valid values that were concerned with the total interests of society and shared by all of its members. He believed in the trend toward the empirical unification of ethical systems: “One might dispute many individual points, the derivation of ethical truth, and the scientific construction of ethical system, but on the most important practical value judgments, good and cultivated people of the same nation in the same cultural age reach agreement more and more” (Schmoller 1911, 494–95).

Third, Schmoller asserted that the ethical approach not only aims at the recognition of moral facts but also is formulated in a teleological form. Teleology is contrasted with causality. In the explanation of a phenomenon teleology focuses on the relationship between an end and means, not between a cause and effects. Teleology appeals to aims in the explanation of human actions and social systems. If a society, a group of individuals, can be regarded as a unified entity with its own aims—in other words, if holism can be assumed—teleological inquiry is possible. Since moral values are to govern a society as a whole, teleology is effective in the study of institutional organization embodying ethics. For Schmoller, the major content of teleology was a principle of justice. He argued: “The economic organization of a nation is not a natural product as was thought for a long time, but mainly a product of current ethical views about what is right and just in relation to different social classes. All progress in economic organization has been so far a triumph of ethical ideas and will continue to be so in the future” (Schmoller [1874] 1890, 55–56).

That ethics plays a system-constructing role in Schmoller's research program can be best understood in terms of the methodological importance of teleology in his thought. He regarded teleology as a heuristic device that supplements an empirical science when empirical knowledge is not sufficient; it assumes that individuals behave as if they would purposefully serve the ends of the whole. According to him: "Teleological investigation is the most important method because it grasps the total of phenomena, whose inner causal relations are not yet known, as a whole. It is similar to a systematic investigation insofar as the latter systematizes and grasps the total of phenomena or truth consistently" (Schmoller 1911, 437). This clearly indicates the methodological aim of Schmoller's teleology, which has nothing to do with the justification of a specific ideology. The aim is to provide a preliminary vision or *Weltanschauung* for the purpose of drawing a systematic picture of the world. Schmoller's teleology is a case of methodological holism. When one deals with the outcomes of individual behavior within a given social framework, as is the case with neoclassical economics, it is appropriate to assume methodological individualism. But there is much room for the use of methodological holism if one is to explain individual behavior and its consequences within a variable institutional framework.

Schmoller's teleology, thus interpreted, would be exempted from the charge that it confuses facts with values or runs the risk of optimistic historical determinism, an idea of the continuous progress of man and society. German historicism culminated in the neo-Kantian dichotomy between idiographic cultural science and nomological natural science, and behind the dichotomy there was the claim of the historical sciences to the teleological understanding about the human world in contradistinction to the natural sciences based on causal explanations.

An important methodological problem then arises: how can a teleological supposition be consistent with empirical research? Schmoller's empiricist conception of ethics is extremely important in this regard; it has two aspects. On the one hand, it is an undeniable fact that values determine human recognition, valuation, and action. One selects certain things as objects of recognition because they deserve special attention from the viewpoint of values. Whenever one values something as very important or desirable, he ranks the object according to a specific value system. Whenever one takes an action, he is motivated and directed by values as the motive and goal. The role of values in recognition, valuation, and action are undoubtedly empirical facts and are subject to empirical research; there is nothing unscientific in treating values as facts. Schmoller contended that these values are embedded in customs, laws, and morals of a society in the form of social and economic institutions. These institutions in turn regulate the economic behavior of individuals in a society. Thus values are imposed upon individuals by society.

On the other hand, there is another facet of the empirical conception of ethics, namely teleology as an organizing principle of social investigation. The mere record of existing morals cannot lead to teleology but only moral anthropology, although such a procedure certainly entails empirical knowl-

edge. Although it is necessary to observe reality and collect materials in the discussion of morality, it is required at the same time to formulate a normative principle and organize the moral reality. For this purpose, deductive construction of theory starting from appropriate assumptions is needed. Like his historical research, Schmoller's ethical approach lacks explicit theoretical formulation. Teleology as methodological holism does not prevent us from understanding moral values in terms of agreement based on the rationality of individuals, as is seen in the tradition of the social contract theory. The relationship between methodological individualism and holism can be explained in terms of two aspects of individual behavior with regard to social norms, i.e., agreement and conformity.

I would like to suggest a way in that one could interpret and reconstruct Schmoller's ethical approach in terms of two major concepts: reflective equilibrium and evolutionary science. First, as Schmoller correctly emphasized, a moral conception such as a principle of justice is worked out for specific social and economic institutions. It is not intended as the application of a general moral conception to the institutions of society, but rather draws upon basic ideas and convictions that are embedded in them. The moral conception is supported by what John Rawls calls an "overlapping consensus" in a society, i.e., a consensus on a political conception that, despite a diversity of religious, philosophical, and moral doctrines, could be attained by a process of convergence or intersection (Rawls 1987). The justification of morality on the basis of self- or group interests cannot be stable. Rawls tried to find a shared basis of agreement underlying specified political, social, and economic institutions. Schmoller's conception of objectively and universally valid values can be seen as parallel to Rawls's conception of an overlapping consensus.

At first sight, a deep disagreement exists on the way basic institutions should be arranged. But at the same time there is an implicitly recognized basis of agreement in our convictions, beliefs, and judgments. According to Rawls, we collect such convictions and try to organize the basic ideas implicit in these convictions into a coherent principle of justice on the basis of value premises, which is also consistent with the shared convictions. Rawls's method of constructing ethical theory is that of "reflective equilibrium," which justifies a moral principle by establishing a coherence between basic value premises, the moral principle, and shared convictions. Therefore, it is the task of ethical theory to articulate intuitive ideas and beliefs so that they can be recognized as coherent with a proposed moral principle and its basic premises.

Second, although Rawls's method of reflective equilibrium is valuable as a framework for theory construction in ethics and should be used to clarify one aspect of Schmoller's ethical approach, it is confined to the establishment of a static state with fixed social, economic, and political institutions. The strength of Schmoller's ethical approach lies in a historical perspective. In contrast to Rawlsian moral equilibrium, Schmoller explicitly considered an evolutionary process based on the interactions between morals and institutions. His teleology provides a basis of evolutionary theory. In a teleological view, the telos of systems and institutions is generally considered to be self-survival and

accounts for the mechanism of their establishment and transformation in terms of the goal-directed behavior of the systems. The teleological explanation of evolutionary process is based on a future goal as an always desired but as yet unattained objective; it cannot predict a future course; teleology only understands a process as we run after it.

If end-means rationality means the conformity of means to goal achievement, evolutionism maintains end-means rationality without end (Spaeman and Löwe 1981). In evolutionism there is no end-means relationship prior to the process of selection; what is useless to survival is removed spontaneously, and as a result of this process end-means rationality will be realized.

It is quite natural that the revolution of an economic system cannot be dealt with in terms of economic theory, separated from history, culture, morality, social structure, and so on. A dynamic economic theory incorporating capital accumulation and technical change is not enough to understand evolving economic institutions. According to Schmoller, institutions consist of two elements, both of which are left out of economic theory: technology and ethics. It is Schumpeter's contribution that technological innovation is regarded as a focal point of evolutionary economics. Yet ethical factors such as customs, laws, and morals were still excluded from economics mainly owing to the narrow conception of value-freedom. But they must be considered as another essential component of evolutionary economics.

The basic scheme of Schmoller's evolutionary economics can be expressed in a simple form. Schmoller distinguished three types of social organizations in a national economy: the family, the local community (city, village, state), and the firms (Schmoller 1900, vol. 1, 53–57). Each type is based on a different organizational principle. In the case of the family, it is sympathy, kinship, and love; in the case of the local community, it is neighborhood, nationalism, law, and coercion; and in the case of a profit-making firm, it is a contract based on private law. What Schmoller meant by the ethical and social determinants of economic institutions actually relates to these principles. According to Schmoller, it is wrong to argue that economic life is always an individual process because it is a technical process of satisfying individual wants. In contrast with the firm, family and community are not established primarily for economic activity. From autarchic family economy or tribal economy developed two types of organizations. On the one hand, organizations of the local community such as village economy, city economy, territorial economy, and national economy were formed for the purpose of controlling economic life and serving the public interest at different levels of the regional economy. On the other hand, firms were developed as an organization to pursue private profits and entailed various institutional arrangements such as the division of labor, markets, social classes, property ownership, and so on.

Schmoller's scheme of development in stages from village economy to city economy to territorial economy to national economy was designed in terms of the regional community as the carrier of social policy in a wide sense that worked to control the free play of firms in markets. The stage scheme was

concerned with the evolution of institutions brought about by the interactions between ethics and economy, between spiritual-social and natural-technical factors. Specifically, the control by guild in city economy, the rule by lord in territorial economy, and the social policy by government in national economy were attempts at the moral binding of an economy. Schmoller's stage scheme basically differs from the schemes of the old German Historical School in his treatment of the ethical aspect of economy in addition to its technical aspects, with which the old Historical School was exclusively concerned. Evolutionary stage theory is located at the intersection of the theory-history axis and the ethics-economy axis in the diagram suggested in the above (section I).

#### IV. Conclusion

I have been concerned with Schmoller's method, approach, and research program rather than his substantive economics in *Grundriss*. Now I want to say a few words about *Grundriss*. The book constitutes a coherent system: it begins with an analysis of the ethical foundation of economy, then discusses two branches of economics, i.e., the "anatomy" of the institutional framework that embodies ethics, on the one hand, and the "physiology" of economic circulation in terms of price and income, on the other, and finally investigates the development of society as a whole. But the lengthy description in *Grundriss* of economic conditions in different times and places is extremely boring and likely to put the basic scheme out of the reader's mind. If the fat were removed from the book so that a skeleton could be brought out in full relief, it could stimulate a theoretical mind to formulate the skeleton relations. Even in light of his research program, which consists of (i) the collection of data, (ii) definition and classification, and (iii) the causal explanation, *Grundriss* has hardly reached the third step. *Grundriss* is not a finished work of the new type of economics proposed by the German Historical School, but rather an accumulation of raw materials in a roughly classified form, on the one hand, and a presentation of the vague but stoutly built scheme of stage theory, on the other. There is a great gap between the enormous bulk of materials and the simple scheme; the former is not fused together to fit the latter mainly because the texture of supplementary functional relations is lacking on the theoretical side. Schmoller did not develop an effective tool to dispose of these materials in order to realize his basic vision concerning morals and institutions.

It is said that Schmoller hindered the development of theory in the sense of neoclassical economics for fifty years in the German-speaking world, but the potentiality of his vision to encourage evolutionary or institutional economics centering on the relationship between morals and institutions has proved to be quite high. I mention a potentiality, because, although contemporary economists have posed an increasing challenge to evolutionary or institutional economics, they know little about the German Historical School as their forerunner. The present criticism of the new institutional economics was already strongly advocated by Schmoller as the critique of classical and

neoclassical economics. The agenda of his historical-ethical approach is worthy of revaluation. From this point of view, I suggest, the best part of *Grundriss* is found not in the description of historical and statistical facts but in the summary and speculative interpretation of relevant phenomena. The following sections in *Grundriss* might constitute a better version of Schmoller's attempt to develop evolutionary economics: Introduction (Items 1–33), Book Two (Items 87, 93, 101, 112–13, 122–23, 131–33, 137–38, 147), Book Three (Items 148–49, 152, 158–59, 169–71, 173, 182–83, 185, 188, 202–3, 205, 213, 219, 229, 236), Book Four (Items 237, 245, 251–53, 272–76).

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## Notes

- 1 The influence of Schmoller in German academics was manifested in the Festschrift for the seventieth and centenary anniversaries of his birth. See Geibel *et al* (1908) and Spiethoff (1938). The positive appraisal of Schmoller on a large-scale ended with the latter Festschrift in 1938. There followed a fifty-year period of complete neglect. However, since the 150th anniversary of his birth in 1988, there has been a growing revival of studies on Schmoller. See, for example, Richter (1988), O'Brien (1989), Balabkins (1989), Schiera and Tenbruck (1989), Bock, Homann, and Schiera (1989), and Backhaus (1993).

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