

Adam Smith on Religion and Economics

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Abstract: Adam Smith has been studied over and over again on issues such as the invisible hand, the division of labor, specialization, free enterprise, etc. However, his contributions to the interface between economics and religion, which are also important, are less well known. Many of these contributions foreshadow such advances in economics as club goods, rational choice, and monopoly theory. The present paper is an attempt to focus on that aspect of this literature.

Keywords: Religion, economics, Adam Smith

I. Introduction

The field of Economics and Religion is starting to gain traction¹ years after its first exposure in Adam Smith's magnum opus *An Inquiry into the Nature and Cause of the Wealth of Nations* in 1776. The *Wealth of Nations* is mostly known for its theories of the division of labor and the "invisible hand" metaphor. He links the self-interest of the individual with the public interest of the entire society. However, Smith and the *Wealth of Nations* are less known for applying economic insights to the analysis of religion and its institutions.² Yet much has been written about this topic. This paper is an attempt to summarize this literature. How best to start this summary? It is with Smith's concept of the "invisible hand." That 18th century philosopher-economist thought that this invisible hand was God's hand.³ There are of course other connections between Smith and religion, see on this below, but that might well be the best summary of this relationship.

Smith's views on religion are elaborated in Book V, Chapter I, Part 3, Article 3 of

1 It has gained so much traction that there are actually two separate scholarly endeavors in this category. One of them treats religion as an industry, and the separate types of churches, synagogues, mosques, etc., as competing businesses. The other, of which the present paper is a part, deals with the economic perspectives of leading spokesmen for these different "firms." A parallel may be found in psychology, wherein very distinct enterprises huddle under this label. For example, experiments with rats on the one hand, and the views of Freud, Jung, Ellis, etc., on the other. But then there is also educational psychology, evolutionary psychology (just to confuse matters, this is also referred to as sociobiology) and social psychology, which are all distinct from running rats through mazes and psychotherapy.

2 See on this the important work of Alvey, 2004, Oslington, 2011, 2012 and Otteson, 2011. See also Otteson 2000, 2002, 2006.

3 Mises, 1949, p. 147, fn. 3, supports this interpretation.

the *Wealth of Nations*. He considers the best method for the funding of religious institutions and states that the subsistence of teachers of these religious institutions depends "upon the voluntary contributions of their hearers, or they may derive it from some other fund to which the law of their country may entitle them; such as a land estate, a tithe or land tax, an established salary or stipend." He then considers the ideal situation for good religious institutions, the downside of the Catholic Church, and the best substitutes for this latter religious institution. These views and insights had been mostly neglected until the 20th century.

The literature surrounding religion and economics sometimes treats the former as an independent variable and sometimes as a dependent variable. According to McCleary and Barro (2006, 49) when "religion is viewed as an independent variable, a key issue is how religiosity affects individual characteristics, such as work ethic, honesty and thrift, and thereby influences economic performance." The most prominent proponent of this theory was Weber (1930), although earlier John Wesley (Maddox, 1998) held similar beliefs.

If analyzed as a dependent variable then the "central question is how economic development and political institutions affect religious participation and beliefs" (McCleary and Barro (2006, 49). Furthermore, if viewed as a dependent variable both can be broken down into supply-side and demand-side models.

Demand-side analysis includes the secularization and rational choice models. Secularization purports that the more developed a country is, the more secular it will be. The rational choice model was applied to religion by Azzi and Ehrenberg (1975).

Because humans weigh costs against benefits, McCleary and Barro (2006, 50) state that “[Azzi and Ehrenberg’s] model implies that time devoted to formal religious services and personal prayer will be high among persons with low value of time...” For example, older people may be more engaged in religious activity because their opportunity cost is low.

In this paper we follow the supply side model of Adam Smith known as the religious market model and his specific argument wherein Smith argues for competing religious organizations. According to McCleary (2008, 1) “permitting any and all religions to be practiced, the lack of state intervention (short of violence, coercion, and repression) creates an open market in which religious groups engage in rational discussion about religious beliefs.”

Rosenberg (1960) was the first modern writer to address Adam Smith and religion. Since then, articles have been written by Levy (1978), Anderson (1988), and others. This work has subsequently led to much debate in the economics literature seeking to test and clarify Smith’s views.

Smith was a pioneer in the field of economics and religion (McCleary, 2008) In his brief writing on this topic in the *Wealth of Nations* Smith manages to touch upon ideas and theories that would be prominent for centuries; for example, club goods theory, competition in the market place and the danger of state and religious affiliation. Sadly, this may be his most neglected contribution to economics.

This paper is divided into five sections in which we visit Smith’s thought, the debate surrounding it and explain the arguments of the different sides. The two main disagreements occur between Anderson’s (1998) interpretation and that of Leathers and Raines (1992). This is detailed in Section II. In

Section III, we incorporate Iannaccone’s (1992) theory of religion as a club good. In Section IV, we deal with Kirznerian and Rothbardian theories of entrepreneurship and monopolies respectively, explain what these have to do with the economics of religion and offer two major pitfalls in Smith’s treatment of religious institutions. Section V, is our conclusion.

II. Different Interpretations

According to Rosenberg (1960) and Levy (1978), Adam Smith believed in competition in religion. However, Rosenberg reads Smith as believing that the price system’s superiority “as a way of organizing economic life lay in the fact that, when it was surrounded by the appropriate institutions, it tied the dynamic and powerful motive force of self-interest to the general welfare” (p. 560). Therefore, the correct institutional structure had to be in place.

Anderson (1988) takes this idea a step further. According to him, “Smith was probably the first ‘economic imperialist’” (p. 1067). This is the name given to those who apply economic principle traditionally thought to be outside the domain of economics. Examples include Buchanan and Tullocks’ (1962) economic analysis of the incentives facing politicians in the political system and Becker’s (1957, 1964, 1974A, 1974B, 1975, 1976, 1978, 1981, 1990) forays into an economic analysis of sex, marriage, crime, discrimination, sociology, human capital, fertility and punishment.

Anderson’s statement is supported by an oft-neglected part of the *Wealth of Nations*. Smith, states Anderson, “was concerned with two basic problems: (1) the economic incentives involved in the individual’s decision to practice religion and (2) the economic effects of different systems of religious

belief as reflected in individual behavior” (p. 1068). Adhering to religious instruction regulates moral behavior, and also results in human capital formation and accumulation. Human capital (Becker, 1964) includes amongst myriad other things knowledge and skills gained through education, or work experience.⁴ In fact Smith (1981 [1776]), states that “The institutions for the instruction of people of all ages are chiefly those for religious instruction” (p. 788)

Smith also favored many small sects rather than few large religious institutions:

“The teachers of each sect, seeing themselves surrounded on all sides with more adversaries than friends, would be obliged to learn that candour and moderation which is so seldom to be found among the teachers of those great sects, who [as a result of legal entry restrictions facing competing sects]... see nothing round them but followers, disciples, and humble admirers. The teachers of each little sect... would be obliged to respect those of almost every other sect, and the concessions which they would mutually find... convenient and agreeable... might in time... reduce the doctrine of the greater part of them to that pure and rational religion, free from every mixture of absurdity, imposture, or fanaticism.... This plan of ecclesiastical government, or more properly of no ecclesiastical government, [would tend to be] productive of the most philosophical

4 We do not want to interpret Smith as an 18th century Chicago rational choice theorist. Placing Smith’s writings in their 18th century context will tend to obviate any such interpretation. See on this Ross, 2010; Winch, 1996.

good temper and moderation with regard to every sort of religious principle.” (p. 793)

Anderson says “this [passage] is probably the closest Smith comes in *Wealth* (or elsewhere) to arguing in favor of free-market anarchism” (p. 1074).

Leathers and Raines criticize Anderson’s argument on the grounds of ambiguity. According to them it is ambiguous whether Smith believed in competing religious markets. Furthermore, Smith viewed established churches as inferior to free religious competition, but spoke favorably of established churches in Scotland, Switzerland, and the Netherlands. Leathers and Raines stated, “Moreover, several points raised in his discussion of established churches tend to qualify or contradict his argument for a ‘supply and demand’ approach to religion” (p. 504).

How can these perceived contradictions in thought be reconciled? According to Ekelund, Hebert and Tollison, (2005, 648), Smith asserted three key propositions. “Smith’s maximand in religious markets was ‘consumer sovereignty.’” Secondly, “Smith recognized that the good demanded (religion) was not homogeneous.” And lastly, “Smith encased his views on religion within his own holist views of history and economics” (p. 648). These three propositions allow the debate surrounding what Smith really meant to be flushed out.

Laissez-faire among demanders of religion was the best choice in Ekelund, Hebert and Tollison’s eye. However, when one, two, or three main religious institutions thrived he analyzed second best alternatives. In this way he was able to say, without contradiction, that “Presbyterianism was not perfect, but it was, from an economic perspective, better than most alternatives” (p. 655).⁵ And Smith

5 We can only speculate as to why he thought this. Perhaps it was because of the popularity of this

confirms this saying, “In [the clergyman’s] own conduct, therefore, he is obliged to follow that system of morals which the common people respect the most” (p. 810).

The alternatives Smith considered included the Roman Catholic, Anglican, and Calvinist churches. These three were organized in a top-down, bureaucratic fashion. Presbyterianism, on the other hand, was structured in a bottom-up manner. Therefore, among the alternatives that existed in Scotland at this period, what appealed most to Smith was the internal organization of the Presbyterian clergy: “The equality which the Presbyterian form of church government establishes among the clergy, consists, first, in the equality of authority or ecclesiastical jurisdiction” (p. 809)

Ekelund, Hebert and Tollison (2005) showed that the debate was founded on inaccurate interpretations. The main question was “...how, under the constraints of establishment could preachers be relieved of indolence and greed while yet maintaining consumer choice and sovereignty?” (p. 654). The institutional mechanism of equality, freedom, etc. of Presbyterianism answered this question most satisfactorily and therefore, “It is accordingly in Presbyterian countries only that we ever find the common people converted, without persecution, completely, and almost to a man, to the established church” (Smith, p. 810).

Summarizing Smith’s views, McCleary and Barro (2006, 50) state that the “literature argues that government regulation and subsidy influence competition among religion providers and thereby affects the nature of the religion product.” While people may still believe in religion and things such as heaven and hell they may not “belong” or attend church. In other words they believe but don’t belong.

Smith may well have preferred the bottom-religion at that time.

up to the top-down management, but as far as compatibility with free enterprise, both are orthogonal. That is, each of these two is as fully consistent with laissez faire capitalism as the other. As long as both are voluntary, and do not engage in crony capitalist initiatives⁶ that give one religious “firm” an advantage over any other, then whether they are centralized or decentralized matters not one whit. The orchestra is a very centrally planned undertaking. There is virtually no scope for initiative on the part of the musicians. The wind players are even told precisely when to *breathe!* In contrast, once the players are out there on the court, basketball and volleyball rely heavily upon individual creativity. Is the one compatible with the free market philosophy and the other not? If that is Smith’s view, it is in error.

III. Club Goods

Recently, Iannaccone (1992), and Berman (2008) have analyzed religion using the club good approach. This theory views religion as an organization or institution that provides club goods. Club goods are non-rivalrous but excludable in their consumption and provide benefits such as religious instruction, and social networking and other such services. The Presbyterian Church may exclude these club goods through some sort of fee, sacrifice, or other method.

States Iannaccone (1992): “Krishnas shave their heads, wear robes, and chant in public; Jehovah’s Witnesses refuse transfusions; Mormons abstain from caffeine and tobacco...” (p. 273).⁷ Although the

⁶ Sometimes called “rent seeking,” but why anyone would want to sully a perfectly legitimate phase as “rent” by linking it to entry restrictions, favoritism and “crony” capitalism is beyond our ken. See on this Block, 2000, 2002.

⁷ The Amish, Chasidic Jews and other religious followers also adorn unique garb.

Presbyterian Church did not do such things, such as being strict Sabbatarians, it was able to gain a foothold because the competing Roman Catholic Church supported much more of these elements.⁸ Furthermore, “Distinctive diet, dress, grooming, and social customs constrain and often stigmatize members, making participation in alternative activities more costly” (p. 276).

Berman addresses sacrifices in his paper stating that “our insights into rebel organizations flow from understanding *sacrifices* – acts that irreversibly destroy value such as circumcision, burnt offerings, or ritual bloodletting” (p. 1952).

It can be said that the Presbyterian church and Protestantism more generally was able to gain its foothold during the Protestant Reformation by doing away with complex rituals that raised the cost of belonging to the Roman Catholic church.

IV. Kirzner and Rothbard

Israel Kirzner has become famous for his pioneering work on the entrepreneur and the market process. He believes that “the driving force behind this systematic process (equilibration of the market) in what will be described below as entrepreneurial discovery” (1997, p. 62). For Kirzner, however, the Austrian market process depends not only on the entrepreneurial role but also on the role of discovery and rivalrous competition.

In a broad sense, Kirzner meant

⁸ The Catholic Church also aligned itself throughout history with states. For example, Charlemagne (“The Christian Warrior”) and the founding of The Holy Roman Empire. It also has engaged in persecutions such as the Spanish Inquisition. However, when it does this it ceases to be a club. See Block (2003), Stringham (2002). Of course, States also aligned themselves with the Roman Catholic Church (or against it). Causality runs both ways here. We owe last point to a referee of this journal.

entrepreneurship as any human action. People act because they believe they have discovered profit opportunities. Here profit need not necessarily mean pecuniary or monetary profit, but could also mean psychic profits. In the view of Kirzner “...each entrepreneur seeks to outdo his rivals in offering goods to consumers (recognizing that because those rivals have not been offering the best possible deals to consumers, profits can be made by offering consumers better deals)” (p. 73). This meshes well with Smith’s statement that:

“[The clergy of an established and well-endowed religion]... are apt gradually to lose the qualities, both good and bad, which gave them authority and influence with the inferior ranks of people, and which had perhaps been the original causes of the success and establishment of their religion.” (p. 789)

Whether they knew it or not, the reformers during the Protestant reformation were entrepreneurs and it is in this environment that the Protestant religion was able to gain footholds in various areas of Europe such as Switzerland, the Netherlands, and Scotland.

Leather and Raines (2008), however, argue that Smith disagreed that all competition among religious sects was beneficial. According to them, Smith believed in a regulatory role of government to ensure that religious fanaticism did not occur. Adam Smith believed the government should both leave religions alone and to make sure religions leave each other alone. In our view, this does not violate free-market competition in religion so long as there is voluntary entry and exit for religious demanders.

The Roman Catholic Church was also notable for the monopoly privileges that were often granted to it. According to Smith:

“Such a clergy, upon such an emergency, have commonly no other resource than to call upon the civil magistrate to persecute, destroy or drive out their adversaries, as disturbers of the public peace. It was thus that the Roman Catholic clergy called upon the civil magistrates to persecute the Protestants, and the Church of England to persecute the Dissenters.” (p. 789)

Kirzner’s second condition was not entirely absent. However, once it did show its head, it was often violently suppressed. “This type of monopoly, stated Murray Rothbard (1962 [2001]), “can never arise on a free market, unhampered by state interference” (p. 591). It is safe to say that the Roman Catholic Church was a monopoly (though not in all places, nor in all regards) because it was granted “special privilege by the state” (p.591).

The Spanish Catholic church, for example, was strongly linked with the state and because of its wealth from South America was able to become stricter with commerce and religion. According to Trevor-Roper (1967):

“The Counter-Reformation State was generalized in Europe, above all, by the power of Spain. It is one of the great accidents, perhaps misfortunes, of history that it was the Castilian monarchy, that archaic “feudal” society accidentally raised to world power by American silver, which stood out, in the sixteenth century, as the champion of the Catholic Church, and thus fastened something of its own character upon both Church and State wherever their combined patronage prevailed.

“This alliance between state and religious institutions Smith mentions in passing. For him, “Times of violent religious controversy have generally been times of equally violent political faction. Upon such occasions, each political party has either found it, or imagined it for its interest to league itself with someone or other of the contending religious sects.” (p. 791-2).

The market cannot have rivalrous competition then, and subsequently “induce dynamic entrepreneurship competition” without open entry to markets (Kirzner, p. 73). The market for religious goods is no less subject to this consideration than the one for automobiles or pens.

The Reformation found fertile soil in Scotland because religious entrepreneurs such as John Knox exploited with great effect free-entry into the religious market.⁹ To wit, “In some countries, as in Scotland, where the government was weak, unpopular, and not very firmly established, the Reformation was strong enough to overturn, not only the church, but the state likewise for attempting to support the church” (Smith, p. 807). Conversely, with their assistance with the government’s assistance “it was enabled, though not without great difficulty and much bloodshed, either to suppress altogether or to obstruct very much the progress of the Reformation in their dominions” (Smith, p. 806).

But Smith’s views on these matters have not been without criticism. Rothbard (1995, 501) criticizes Smith on many grounds including that of entrepreneurship. According to Rothbard, Smith’s “exclusive attention to

⁹ We have no evidence that this was easier in Scotland because of ill-feelings toward the English, and the link between the latter and the Roman Catholic and later Anglican churches. However, we regard this as highly plausible.

long-run equilibrium led [him] to toss out the entire entrepreneurship-and-uncertainty approach.”¹⁰

Ahiakpor (1999), however, maintains that Rothbard misinterprets Smith on entrepreneurship (amongst many other issues). Ahiakpor (1999, p. 361) says “Yet Rothbard credits Smith with pointing out that ‘the capitalist (the ‘undertaker’) *reaps profits in return for the risk*, and for interest on the investment for maintaining the workers until the product is sold- so that the capitalist earns profit for important functions.” Smith veers from the path in that he says “There are two very easy and effectual remedies, however, by whose joint operation the state might, without violence, correct whatever was unsocial or disagreeably rigorous in the morals of all the little sect into which the country was divided” (p. 796). Immediately questions arise. Who is to decide what is unsocial? How is the state to “without violence” correct whatever it is that is unsocial, disagreeably rigorous, etc.? Smith suggests “the state might render almost universal among all middling or more than middling rank and fortune... probation... to be undergone by every person” for such and such a profession (p. 796).

V. Conclusion

We have detailed Smith’s stance on religious competition and his belief in it. The debate that arose based on his remarks has

10 Why is this section on entrepreneurship of relevance to our inquiry regarding Smith and religion? The link is that the essence, at least for us, of the connection between Smith and religion is his thought that the invisible hand is God’s hand. However, in turn, the key element of the invisible hand is entrepreneurship. It is the entrepreneur, not anyone else, who is led by his self interest, his seeking after profits, to promote the public good. So, it is crucial, for our analysis, to delve into Smith’s views of the entrepreneur, and critiques of it, and also defenses of it.

made significant strides in clarifying matters. However, these issues are at best still only incompletely resolved.

The organization of the Presbyterian Church greatly appealed to Smith as a second best alternative in his theory of freely competing religious organizations and helped to demonstrate why the religious institutional structure was developed as it was.

We analyzed why the Presbyterian Church took hold in Scotland. The Roman Catholic Church had a monopoly in many places in Europe, but, Scotland was able to fight back because it was more freely open to competitive entry. This history fits nicely into a Kirznerian and Rothbardian theory of entrepreneurship and monopoly.¹¹

For all his work on behalf of the free marketplace, Smith did not completely rule out a beneficial positive role for the state. He believed the government could furnish a link between the self-interest of the individual and the public interest of society as a whole. His non-state institutional mechanisms may have provided the answer to his failure to fully support free enterprise.

These non-state institutional mechanisms (competing religious organizations providing club goods, entrepreneurs seeking alternatives to those consumers didn’t desire, etc.) have helped support arguments for anarchism. The state does not need to push for human welfare; it already moves in that direction better than any other institution.

Modern economic theory has further elaborated, debated and supported the economic analysis and conclusions about religion that were first formulated in Smith’s *The Wealth of Nations* in 1776, so his views don’t seem out of place even in the modern era. He hinted at the foundation of club-

11 The latter two economists actually diverged with regard to their theory of monopoly. See on this Block (1977).

good theory by putting forth the view that individuals join organizations because of the goods they receive from membership and he foreshadowed treating the church or religious institution as a firm subject to the same laws of the free-market as any other. Both of these advancements would combine in the present day subfield of Economics and Religion.

These developments mentioned here should only serve to bolster Adam Smith's

reputation as anticipating recent work in economic thought, including in the field of the economics of religion. (As Viner said, "It's all in Adam Smith.") Although "sophisticated" theories with highly mathematical language may have become the norm in economics, the fact remains: Adam Smith's economic analysis, and many of the greatest additions to it, is strictly qualitative, and yet very much adds to our store of economic analysis.

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