

Adam Smith and the Wealth of Nations

The spirit of freedom and confidence expressed in the American colonies during the mid-1700s reflected a fresh, optimistic, and vigorous view of life held by an increasing number of people. Traders and manufacturers had grown impatient with the existing mercantilist system. Business operators felt frustrated and hindered by the direction and control of economic life exercised by the national government. They wanted more freedom to pursue their own personal advantage. Many people felt they were not getting the rewards to which their efforts entitled them. Instead they felt the rewards went to the state.

Such persons believed that by seeking their own advantage in business the entire nation would prosper. In other words, by helping oneself one helped the nation. This new feeling was best expressed by the Scottish economist and philosopher Adam Smith (1732-1790). His book *The Wealth of Nations*, published in 1776, captured the imagination of Europe and America and became, by far, the most influential work ever written by an economist. Smith's philosophy of freeing merchants and traders from restrictions was called *laissez faire* (literally, "allow them to do" or "leave alone"). It dominated economic thought for the next 150 years,

particularly in the young and ambitious colonies.

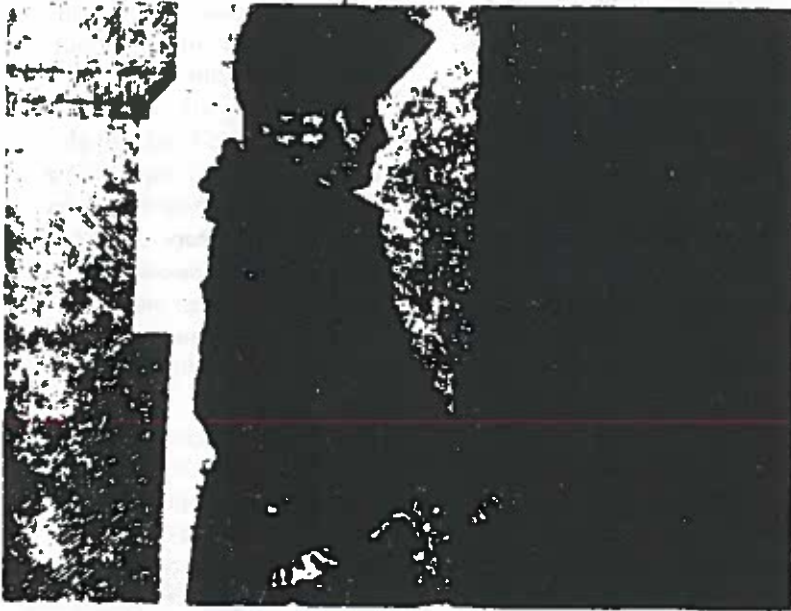
Adam Smith believed, along with the writers of the U.S. Constitution, that human behavior followed certain "laws of nature." (These were the same "Laws of Nature and of Nature's God" that Thomas Jefferson appealed to in the Declaration of Independence.) One of these laws was self-interest. Smith believed that people engaged in trade and manufacturing for their own profit—not for the sake of the nation or to benefit others.

Personally a charitable man, Smith nevertheless believed that the selfish foundation of business activity was actually a good thing. In a nation where everyone was allowed to seek his or her own personal advantage, everyone would automatically also contribute to the prosperity of the nation. The skilled worker who could command high wages, the manufacturer of cheap goods, and the trader who selected merchandise that would please customers—all were seeking their own profit. But they were also performing a useful service and benefiting society as a whole. It is as if an "invisible hand" were turning individual self-interest into the common good. A well-governed nation, Smith believed, would encourage the natural forces of self-interest, limiting them only

when they violated the principles of justice.

Mercantilism, the economic system which dominated Europe in Smith's day, represented the opposite of what he considered a natural system. In *The Wealth of Nations*, Smith blasts not only the mass of mercantilist controls over commerce but also the monopolies and privileges granted by governments to certain groups and individuals. These, he believed, only frustrated nature. Without the rivalry of other competitors, the privileged traders, producers, and merchants grew lazy and smug. This resulted in shoddy goods, lower profits, and finally a poorer nation.

Calling for an end to mercantilism, Adam Smith proposed a free choice of occupations. He urged the abolition of government apprenticeship rules and laws restricting settlements in certain parts of the country. He attacked duties, bounties, and the monopolies of chartered companies, such as those that operated in the British colonies in North America. However, even as he denounced these hindrances to trade, Smith realized that they played a crucial role in the British economy of his day. With this in mind, he advised that they should be lifted gradually whenever a quick repeal would cause serious unemployment. He also thought that it



Adam Smith, the Scottish economist, gave support to the idea of human progress through individual efforts.

was unrealistic to expect that a completely free trade or laissez-faire system would ever be established in Great Britain.

In Book V of *The Wealth of Nations*, Smith discusses the role of government in a laissez-faire society. He restricts the government to three functions: (1) national defense, (2) the enforcement of laws protecting life and property, and (3) the construction and maintenance of public works that might be highly useful but not profitable enough for private builders. Under this last heading, he included roads, bridges, canals, harbors, and, to some degree, schools.

It is clear that, for Smith, the government's participation in the affairs of the nation should be very much the exception rather than the rule. The simple

system of "natural liberty" would, in his view, suffice in dealing with most of a country's problems.

As with the thoughts of many influential thinkers, Smith's ideas were used by some to suit their own purposes. For example, in the 1800s, manufacturers wanted no state interference in employer-employee disputes. Yet, some of these same manufacturers urged the state to pass tariff laws to block the importing of competing goods. They thus defended the policy of laissez faire only when it was convenient.

Despite these questionable uses of Adam Smith's theories, *The Wealth of Nations* stands as a groundbreaking work which almost alone established economics as a respected science. During the 1800s, Smith's ideas

also served to spur the industrial development of such countries as England, France, and the United States.

Had Adam Smith published *The Wealth of Nations* earlier than 1776, it is quite possible that the American Revolution would never have taken place. Mercantilist measures, such as the Navigation Acts or the Molasses Act, angered American colonists and inspired thoughts of revolt. Smith, of course, called for the repeal of this type of interference in trade. "Great Britain," he wrote, "derives nothing but loss from the dominion she assumes over her colonies." Smith proposed a free trade association of independent countries in which Britain and the former colonies cooperate as "faithful, affectionate, and generous allies." But by the time these sensible proposals were published, the conflict between Great Britain and the American colonies had already begun.

Understanding Free Enterprise

1. If Adam Smith's *Wealth of Nations* had been published a few years earlier, do you think it might have changed the history of Britain and its colonies? Give reasons for your answer.
2. According to Smith, why was competition desirable?
3. Are there any U.S. government policies today that could be called mercantilist? Explain.

— Mercantilism - nations seeking wealth & power by gathering colonies; the more colonies, the more benefits to the "mother" nation (Smith hated this)

— Law of Self Interest - an individual engages in business for the benefit of himself... however, this business person will offer goods/services that will benefit others

— Laissez-Faire - govt should stay out the affairs of business

— Rivalry is good

— Govts roles -

1. national defense

2. enforce laws

3. maintain public works

Adam Smith importance

- 1) Smith put into words many of basics of capitalism
- 2) Smith is very popular w/ people who favor capitalistic systems, free enterprise and open markets
- 3) Smith's view about the small size and duties of government is very conservative in nature

Marxism

vs

Smith-ism

- Socialism/
Communism

- big Govt. style

- govt. ownership

- govt. involvement

- elimination of
classes, classes
are unfair

- contracts regulated
and limited

- rivalry eliminated

- interest of the
"greater good"

- man made "Utopia"

- Equal Outcomes

- Capitalism

- limited Govt. style

- private ownership

- Laissez-Faire

- social mobility
is okay, individual
can/free to pursue
any level of success

- freedom of contract

- rivalry is good

- Law of Self Interest

- Laws of Nature

- Equal Opportunities