

# The tercentenary of

This year marks the 300th anniversary of the birth of Adam Smith, the Scottish economist and philosopher. In this article Helen Paul explores the history and important works of the ‘father of economics’

Adam Smith was born in 1723 and so 2023 marks his tercentenary. Smith was hailed as an important thinker in his own lifetime, and he is now thought of as the father of modern economics, particularly for his book *The Wealth of Nations* (1776). While he is a famous name, many people are only familiar with a broad-brush outline of his contributions and his ideas are even taken out of context at times. Smith was interested in moral philosophy and stressed the importance of ethical behaviour in economic decision-making. Three hundred years after his birth, this article addresses his legacy.

## Who was Adam Smith?

Adam Smith was born in the Fife town of Kirkcaldy, in Scotland. He was able to attend a good school in his hometown where he learned subjects such as mathematics and Latin. From there, he went to the University of Glasgow. Smith later won a scholarship to Balliol College, Oxford, where he continued his studies in philosophy. He gave a series of public lectures at the University of Edinburgh and then taught moral philosophy at the University of Glasgow. Later in his career, he was tutor to a young aristocrat and was able to travel around Europe with him. On his travels, Smith met

many of the major European thinkers of the day.

## *The Wealth of Nations*

This may seem a strange beginning for someone who went on to become an economist. However, economics was not yet a separate discipline. Instead, the term ‘political economy’ was used. What we now think of as economic questions, such as how the economy should be organised, were then seen as part of politics or philosophy. The publication of *The Wealth of Nations* marked the beginning of economics as a separate subject — the full title is *An Inquiry into the Nature and Causes of the Wealth of Nations*. Unlike many modern textbooks, it does not rely on the use of algebra or diagrams. Instead, Smith discusses how the economy works in great detail but without many of

the tools that current students of economics are familiar with. For example, there are no supply and demand diagrams in the book as they had not been invented yet. Nor does Smith use much data to back up his arguments. Modern readers might be surprised by this.

Smith was writing for an educated readership, but not a specialist one. Without complicated mathematical models, *The Wealth of Nations* was accessible to a wide range of people. It promised, as its title suggested, to explain why some countries were rich and others were poor. The book was a publishing success and ran to several editions. Indeed, it is still in print today. Whether all of the people who purchased the book read it thoroughly is a different question. It became one of the books that educated people felt the need to place on their bookshelves and its popularity confirmed Adam Smith’s status as one of the most important thinkers of his day.

*The Wealth of Nations* was originally published in two volumes and is a lengthy work. Economics students today are only taught a small proportion of what Smith actually wrote. There are several key ideas that are still associated with him — the division of labour, the concept of absolute advantage, the role of self-interest and the doctrine of laissez-faire.

## The division of labour

The theory of the division of labour posits that if people split up tasks between themselves,

### SPECIFICATION LINKS

how competitive markets work, specialisation and trade, the division of labour, international trade and protectionism



# Adam Smith

they can become more productive overall. In other words, generalists are less effective than specialists. Specialists become more proficient through repeating the same tasks — they find new methods and develop new tools. In addition, it is beneficial to assign people to the tasks that they are good at.

Adam Smith did not think of this theory himself, but he popularised the idea through his book. He also used an example that had already been employed elsewhere — the pin factory. Smith asked his readers to imagine a factory that made pins. Nowadays they are made by machines but in Smith's day, they were made by hand by skilled craftsmen. In order to make one pin, a number of different tasks needed to be performed. For instance, the wire that makes up the body of the pin needs to be made, then it needs to be cut to the correct length. The head of the pin must be crafted separately, then joined to the body. If one person tries to perform all these tasks, then the total output of pins will be very small. The pin maker must keep changing tools for a start. If there are several pin makers all trying to use the same tools and the same materials, then the pin factory will not be very productive. But the workers can be reassigned so that each has his or her own task to perform. Each worker would then become more skilled in that task and the team as a whole would become more productive.

These same ideas of division of labour became very important in the factory age of the later eighteenth and nineteenth centuries. Factories relied on teams of workers who specialised in particular tasks. Critics of factory work, such as Karl Marx, argued that people lost a range of other skills and were left with unfulfilling, repetitive work. Nevertheless, the success of the factory regime seemed to validate Smith's ideas.

In 2007, the Bank of England issued a new £20 banknote to commemorate him. It showed his portrait alongside workers in an eighteenth-century pin factory and included a quotation from *The Wealth of Nations* that read, 'The division of labour in pin manufacturing: (and the great increase in the quantity of work that results)'.

## Absolute advantage

Adam Smith was born into a world where the prevailing approach to international trade was mercantilism. Mercantilists thought that countries needed to export as many goods as possible but import as few as possible. They wanted to erect barriers to trade such as taxes on imports (called tariffs) or ban certain imported goods. This approach is called protectionism. It can lead to trade wars, as countries start to retaliate against each other's trade barriers. In Smith's day, trade wars quickly became real wars. Smith believed that ultimately free trade would bring about a better allocation of resources and a wealthier society.

He was the first person to describe the concept of absolute advantage in international trade. To simplify matters, he used labour as the only input. Suppose that Country A uses fewer labour hours than Country B to make good X. Conversely, Country B uses fewer labour hours than Country A to make good Y. Country A has an absolute advantage in making good X, while Country B has an absolute advantage in making good Y. Smith would argue that both countries should specialise in what they are good at and then trade. The total output would be greater. This is somewhat similar to his arguments for division of labour.

Mercantilists often also believed in bullionism, which suggests that a country should build up reserves of precious metals such as gold and silver, i.e. bullion. Early modern economies still relied on commodity money, which is made from a material that has its own intrinsic value.

In Europe, that meant precious metals like gold and silver. Therefore, bullionists wanted exports to be paid for in commodity money. Foreign coins which came into the country could then be melted down into bullion. In order to stop an outflow of coins from the country, bullionists demanded that imports be reduced to a low level. Adam Smith countered this view arguing that policymakers should consider how people within the country used goods and services, rather than focusing on the country's reserves of precious metal. The wellbeing of the people was the true measure of the country's wealth.

## Self-interest and laissez-faire

Adam Smith was, by training, a philosopher and deeply interested in promoting ethical behaviour. Unfortunately, his ideas about self-interested behaviour in the economy have been misinterpreted. He was not advocating selfishness, but recognising that economic agents respond to incentives and try to maximise their own payoffs. There is a very famous quotation from *The Wealth of Nations* about this idea. It reads:

It is not from the benevolence of the butcher, or brewer, or the baker, that we expect our dinner, but from regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages.

Smith argued that society as a whole benefits if people are properly motivated to work. The theory can be used in many ways,

Today, economics students are taught only a small proportion of Smith's original two-volume *Wealth of Nations*



## KEY POINTS

- 1 Adam Smith is considered the father of economics, as he founded the discipline. His work and ideas are often misinterpreted, and there is still debate around some of his theories.
- 2 Two of his most famous books are *The Wealth of Nations* and *The Theory of Moral Sentiments*.
- 3 Smith is most known for his ideas on the division of labour, the concept of absolute advantage, the role of self-interest and the doctrine of laissez-faire.
- 4 The division of labour theory proposes that workers are more efficient if they are specialists, i.e. they specialise on a particular task rather than all of the tasks required to create a good.
- 5 He suggested the idea of absolute advantage in international trade, whereby countries could benefit by specialising in producing a good and trading with other countries that specialised in different goods, rather than taking a protectionist approach.
- 6 Smith also argued that people respond to economic incentives and that society benefits if they are motivated to work. He also suggested that markets will produce better outcomes than government interventions, although the extent of this is open to debate in his work.

He was also the author of *The Theory of Moral Sentiments*. In this book, he argued for altruistic behaviour and sympathy with others. Smith evidently struggled to work out exactly how much markets should be left to their own devices and how to stop self-interestedness becoming selfishness.

### Three hundred years later

There is still an ongoing debate about many of Smith's ideas. In education and training, there are repeated arguments about how much students should specialise and when. Societies still struggle to work out how much the market can be left to itself. Many popular politicians are protectionist and reject Smith's views on free trade. Adam Smith, like all great thinkers, is often used to justify particular standpoints. His work is often simplified to achieve that end. Smith's ultimate contribution may not be the discussion of particular ideas, but the foundation of a separate discipline of economics.

for example to criticise communist regimes. People will not work hard if they cannot see how they and their children will benefit. Therefore, to produce output under communism often means resorting to force and too much government intervention. Most people will not simply work 'for the greater good'.

Smith also appears to be advocating that governments can leave people to their own devices. The market will produce a better outcome than any government design.

This concept is called 'laissez-faire', which means leaving things to their own course. In the case of economics, laissez-faire means leaving the market to sort itself out.

Free marketers often cite Adam Smith as one of their inspirations. For example, The Adam Smith Institute is a think-tank committed to promoting free markets and reducing the size of the state. However, theorists also talk about the 'Adam Smith problem', which refers to the fact that Smith contradicts himself within his writings.

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