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# The Wealth of Nations

Adam Smith

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An Inquiry into  
the Nature and Causes of  
*The Wealth of Nations*

BY  
ADAM SMITH

With an Introduction and Notes  
by Jonathan B. Wight

# Introduction

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*The Wealth of Nations* is a treasured classic of political economy. First published in March of 1776, Adam Smith wrote the book to influence a special audience—the British Parliament—and its arguments in the early spring of that year pressed for peace and cooperation with Britain’s colonies rather than war. Smith’s message was that economic exploitation, through the monopoly trade of empire, stifled wealth-creation in *both* home and foreign lands. Moreover, protectionism preserved the status quo, and privileged a few elites at the expense of long run growth. Smith wrote, “It is the industry which is carried on for the benefit of the rich and the powerful that is principally encouraged by our mercantile system. That which is carried on for the benefit of the poor and the indigent is too often either neglected or oppressed.”

Smith was a Scottish reformer whose sympathies lay with downtrodden working people. *The Wealth of Nations* was a polemic on the basic rights of human beings to improve their material lives in ways that promoted freedom and dignity. Smith wrote:

*To prohibit a great people, however, from making all that they can of every part of their own produce, or from employing their stock and industry in the way that they judge most advantageous to themselves, is a manifest violation of the most sacred rights of mankind. (p. 372)*

Smith had an inspired vision: that allowing the common person the freedom to express himself through market activities would unleash a creativity and ingenuity that would stun the legislators. Indeed, various countries have tried this experiment, notably China. While millions of peasants starved to death in the misnamed “Great Leap Forward” of central planning in the early 1960s, the loosening of state controls after 1978 triggered a surge of output in small private plots. Likewise in India after liberal reforms began in 1991, output and wealth-creation soared. More mundanely, the freedom to create and trade via the internet has generated a flood of start-up businesses, non-profit organizations, and blogs for people seeking merely to express themselves.

Yet we should quickly (and wisely) note that wealth creation is not Smith’s only, or even ultimate, objective. Humans—in Smith’s mind—are not the grubby creatures of *homo economicus* often depicted in economics textbooks. Rather, humans make complex choices within social groups. A community of people pursuing their own good must grapple with the meaning of justice; they must promote institutions of self control so their self interest does not degenerate into selfishness. In his writings, Smith develops at length his conception of how ethical deliberation arises in a good society.

Readers of this book may be surprised to discover that Smith anticipated and shared many concerns about capitalism (although his term for it was “commercial society”). He worried about the power that big corporations could have in conspiring to create cartels. He noted

that investments vital to the public interest might not be undertaken if profit were the only motive. He did not think the market system was perfect; it needed reasonable regulation to ensure the public safety and well being. Nevertheless, Smith defended markets because he thought they were generally the most reliable mechanism for lifting people out of poverty. Thus, he levelled some of his harshest criticisms at employers whose constant aim seemed to be to depress the wages of workers. By contrast, Smith advocated paying workers higher wages to promote better health and productivity, and he also supported a system of joint public-private education to prevent repetitive labour from degrading workers' human capital.

While Smith was cynical about the motives for state intervention, he acknowledged a legitimate role for government when private interests diverged significantly from the public's interest. Generally, however, Smith believed that a "great society" would flourish best in a "system of natural liberty" in which government focused on executing three duties of great importance—namely, providing for the national defence, establishing a fair system of justice, and carrying out public works.

Some current critics of globalisation claim that exploitation lies at the heart of exchange between rich and poor countries. *The Wealth of Nations* attacks colonialism and mercantilism on these grounds. Smith presents a vision of economic development from the bottom-up, with competitive markets providing the means by which the working poor around the world can improve their skills and living standards. To Smith, concern for people on the low rung of the economic ladder requires not platitudes and handouts, but pragmatic action to break down local systems of exploitation that arise from monopoly. Giving people the opportunity to succeed develops self respect rather than numbing dependency.

We turn to a discussion of Smith's life, his other major works, some key concepts, and the contents of the book.

## Life and works

Adam Smith was born in June 1723 in the fishing village of Kirkcaldy, Scotland, a few months after his father's death. His widowed mother raised him alone and saw that he received an excellent primary education. He pursued further studies at the University of Glasgow, graduating in 1740 under the tutelage of the noted moral philosopher Frances Hutcheson. Preparing for a life in the ministry, Smith travelled to Balliol College, Oxford, to start the period that would rank as the lowest point of his life. Not only were Scots discriminated against in England during this time of rising political and religious passions, but Smith's tutors were narrow-minded and lazy. Smith later castigated Oxford and its faculty (see the Notable Quotes appendix).

After completing his degree, Smith abandoned the ministry and returned to live with his mother in Kirkcaldy. He continued his studies and after a few years made his way to nearby Edinburgh where his entrepreneurial spirit manifested itself in a series of public lectures on rhetoric and other topics for fee. Smith enjoyed a growing reputation that led to his friendship with David Hume, who became his closest friend. In 1751 Smith was elected professor of Logic and Rhetoric at the University of Glasgow, and the following year he accepted

its Chair of Moral Philosophy. Smith's course in moral philosophy included lectures on natural religion, ethics, jurisprudence, and political economy (the latter providing the future foundation for *The Wealth of Nations*). Smith rose to the rank of vice-rector (or provost). These thirteen years as an academic were to be the happiest and most productive of his life.

While modern readers may know of Adam Smith because of *The Wealth of Nations*, his early renown during his life came from *The Theory of Moral Sentiments* (1759), a book that addresses the ethical foundations of human society. The work provides the core of Smith's moral philosophy, and its understanding is essential for discerning some of Smith's economic ideas. The book sold well, leading Hume to quip that this "melancholy" news could only mean the book must be of dubious quality! Based on the reputation of this work, Smith was offered a position as tutor to the stepson of Lord Charles Townshend, the Duke of Buccleuch. This afforded Smith the opportunity to travel to Europe for several years, where he met Voltaire, Francois Quesnay, and other leaders of the Enlightenment movement.

In 1767 Smith received a life pension from the Duke and returned to his mother's home in Kirkcaldy. Inspired by the French reformers he had met, Smith began to develop his Glasgow economics lectures into a book on commerce. This was a slow and painful process, marred by melancholia, hypochondria, and a perfectionist streak that delayed publication. When the book finally appeared in 1776 it came too late to play a decisive role in the tumultuous events leading to war in the American colonies. Intellectuals greeted the book with acclaim, but British legislators were not swayed. *The Wealth of Nations* did give comfort to the colonial revolutionaries, however, as attested by the number of America's founding fathers who bought it for their libraries.

Smith had come to London to be closer to his publisher and to Parliament, but returned to Scotland and entered temporary retirement. He began work on a book about the arts, and planned another on jurisprudence. In 1778 Smith moved to Edinburgh to accept an appointment as Commissioner of Customs for Scotland. There is some irony in this as Smith—a proponent of limited government—became a bureaucrat responsible for collecting taxes for the state. This is less inconsistent than it might appear. Smith didn't take the position for power or money (he still had his large pension and he generously gave away much of what he did make). But he knew that government must raise revenue to pay for legitimate services. Smith was ardent in fulfilling his duties, going so far as to burn some of his wardrobe items when he belatedly realized they had been smuggled into the country. The idealist for free trade was an even greater proponent of duty and justice.

Smith also made time to issue revised editions of *The Theory of Moral Sentiments* and *The Wealth of Nations*. He died July 17, 1790, leaving instructions to burn his unfinished manuscripts. One exception was the *Essays on Philosophical Subjects*, which was published posthumously in 1795. This work contains a number of Smith's important articles on science, the arts, and metaphysics. It also contains a contemporaneous biography of Smith by his friend, Dugald Stewart.

We now turn to Smith's account of morals and their relation to markets.

## Smith's moral philosophy

*The Theory of Moral Sentiments*, Smith's first book, is an account of how humans are adapted by nature to live in society, and how an individual comes to develop a moral conscience—requisite for society to function in reasonable harmony. Smith's thesis is that natural instincts guide action, even if we are not fully conscious of them. Smith writes:

*Thus self-preservation, and the propagation of the species, are the great ends which Nature seems to have proposed in the formation of all animals.... But though we are in this manner endowed with a very strong desire of those ends, it has not been intrusted to the slow and uncertain determinations of our reason, to find out the proper means of bringing them about. Nature has directed us to the greater part of these by original and immediate instincts. Hunger, thirst, the passion which unites the two sexes, the love of pleasure, and the dread of pain, prompt us to apply those means for their own sakes, and without any consideration of their tendency to those beneficent ends which the great Director of nature intended to produce by them.* (Oxford University Press, 1976, p. 77)

Smith identified three main instincts that spur behaviour: the instinct to promote our own wellbeing, the instinct to promote the wellbeing of others, and the instinct to cause harm to others. Our moral conscience passes judgment on these urges. A properly-socialised person comes to see himself as no better than any other person; he comes to hear the rebuking voice of an "impartial spectator" if he improperly places his own interests ahead of others. In *The Wealth of Nations* Smith focuses on the virtuous aspects of properly attending to our own instinct for self-betterment, but it would be incorrect to assume that we can ignore the other instincts in the economic realm. This is because all the instincts serve the interests of society. The institution of justice, for example, arises out of our instinct to seek revenge against people who have wronged us. When the instinct for our self conflicts with the positive and negative instincts for others, Smith's moral sentiments model advises that we must learn self control to adjudicate action.

To summarize, Smith felt that hidden forces called instincts were the impetus for much human behaviour. He labels these invisible instincts the "call," the "power" and the "passions" of nature. At various places he calls them the "invisible hand," a topic to which we now turn.

## The invisible hand

One of Smith's main contributions to economic theory is the concept of the invisible hand. He borrowed the phrase from Shakespeare, Daniel Defoe, and others, but used the term sparingly—once in *Moral Sentiments*, once in *Wealth of Nations*, and once in an earlier essay. However, the idea behind the invisible hand appears throughout his works, namely, that there are hidden forces at work in human society (just as gravity and electricity work invisibly in the material world). These natural instincts, Smith posits, spur us to create order and progress in our communities, even though we are largely unconscious of the motives

for it. We can witness an analogy in wildlife, in which birds construct a nest and fortify it, without having made a logical or reasoned decision to do so. As noted, the human instincts are not simply for self interest, but also for the wider aims of sociability and justice that are necessary for us to live peacefully in society.

When the instincts work compatibly with human institutions, society progresses. For example, the most famous use of the term “invisible hand” occurs in *The Wealth of Nations*, in a chapter where Smith grapples with the issue of whether restraints on trade would harmonise private interests with the public interest. Smith’s analysis is that no intervention is desirable because business traders have a preference to keep their capital at work in the home country anyway. This is because, in the domestic business environment, a merchant “can know better the character and situation of the persons whom he trusts, and if he should happen to be deceived, he knows better the laws of the country from which he must seek redress.” Hence, merchants will put capital to work in their home market for uses that produce the largest value and return. Thus, when every entrepreneur pursues his own self interest in this circumstance, the result is favourable for Britain’s economic growth because capital stays in the country and generates the greatest number of jobs and security:

*By preferring the support of domestic to that of foreign industry, [the merchant] intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. (p. 293)*

Smith argued that in this situation society could progress by removing government barriers and allowing economic actors the freedom to pursue their instincts for self betterment, secure in the belief that this would generally advance society’s goal of economic growth. It is important to remember that the environmental determinants Smith cited, which gave rise to this outcome, were the existence of social capital (trust), competitive markets, and a workable system of justice.

However, institutions can become outmoded and vested interests can stand in the way of development. Smith provided the example of primogeniture in feudal society, which initially served to protect the community’s power and security, but which outlived its usefulness by concentrating land in unproductive hands. Primogeniture penalises the industrious in favour of the lethargic because the instinct for progress is weakest among people who don’t need to work to succeed. Hence, to Smith, “[N]othing can be more contrary to the real interest of a numerous family than a right which, in order to enrich one, beggars all the rest of the children.” (p. 250)

Throughout *The Wealth of Nations* Smith similarly castigates the institution of mercantilism, which promotes the businessperson’s instincts to monopolise markets, thereby damaging society’s interests. In another case, in *The Theory of Moral Sentiments*, Smith lambastes dictators for unleashing their unchecked instincts on humanity, a situation made possible by the institution of autocratic rule. In all these cases the natural instincts that are the invisible hand do not produce beneficial results because institutional circumstances do not harmonise private interests and incentives with the public interest.

This discussion should make clear that to Smith the invisible hand means human instincts, which at times will work harmoniously to produce progress in the right institutional setting. When Smith argued that self interest gives rise to unintended benefits to society, it was in the context of competitive markets, property rights, social capital, and basic institutions of justice. The invisible hand does not mean greed or selfishness, which were behaviours Smith denounced. Nor does the invisible hand mean market efficiency (a modern view). The invisible hand is at work in any institutional setting, even one of central planning (in which people instinctively compete for resources in an inefficient, and likely unfair, process). The human instincts that comprise the invisible hand can be a destructive force in the wrong institutional setting, and must be controlled by a decentralizing power, such as democracy or economic competition. To some readers of Adam Smith, the invisible hand also requires a Benevolent Deity, whose spontaneous order unfolds over time.

## Modern revival

In the present era a renaissance of interest in Adam Smith is underway. The reasons for this are complex, encompassing new scholarship and changing political and economic scenes. *The Wealth of Nations*, once considered outdated during the rise of communism, has regained its luminary status—and rightly so. Central to its resurgence is the notion that Smith's insights into economic systems and the forces of globalisation are highly relevant for our times. Prosperity through markets is an idea that lights the way to lift billions of people out of poverty. Yet we must acknowledge that Smith's appeal for market access for the world's poor remains an unfinished reform effort in many places.

As a technical economist Smith's contributions have been superseded by the advance of economic science. His systematic approach remains the cornerstone of the discipline, but some of his notions are quaintly outmoded, even as they appeared advanced in his own day. For example, Smith criticised the physiocratic view that agriculture was the only source of wealth, noting that manufacturing could certainly also produce value—yet he continued to classify service workers (such as physicians, musicians, and soldiers) as “unproductive” because they produced nothing tangible! Smith's model of prices was ingenious and complex, entailing a “natural” price toward which market values always headed, allowing for the dynamic entry or exit of labour and capital from alternative endeavours. Yet Smith's labour theory of value could not explain the great divergence between the use value of a product and its exchange value (a controversy known as the “diamond-water paradox”—resolved a century after Smith's death by marginal utility theory). Smith's classical view also envisioned full employment as a natural feature of long run equilibrium, and thus seemed irrelevant during the great labour upheavals of the 1930s. Finally, Smith's model of economic development, based on division of labour, trade, and capital accumulation, failed to consider the critical contribution of technological innovation.

From history's vantage, these technical failings are more than compensated for by the great system of thought that Smith bequeathed us. His analytical approach attempts to reveal the connecting principles of nature and to demonstrate the hidden interdependence among economic variables. Discovering and highlighting the unintended consequences and foolishness of human policies is a particular strength of Smith's treatment, painted on a rich historical and institutional canvas.



More than anything, Smith is remembered for articulating a manifesto in support of the “natural system of liberty,” in which prudence, equality, and justice find expression in markets. Smith appeals to us as a hard-headed economist who values the sacred rights of working people over elite special interests. Yet Smith is an idealist rather than an ideologue, pragmatically arguing that reasonable systems that work tolerably well are preferred to perfect, but unattainable, arrangements. Smith is optimistic that, over the long haul, our invisible instincts for order and progress can overcome innumerable obstacles—many self inflicted. He asserts:

*The natural effort of every individual to better his own condition, when suffered to exert itself with freedom and security, is so powerful a principle, that it is alone, and without any assistance, not only capable of carrying on the society to wealth and prosperity, but of surmounting a hundred impertinent obstructions with which the folly of human laws too often incumbers its operations... (p. 349)*

Finally, and importantly, Smith reminds us that an economic process operates within a moral framework. It is not a mechanical engine but a social organism. Virtue requires balancing the sometimes opposing instincts for self and others—and developing the self control that is usually preferable to state control.

Smith’s brilliant rhetoric, combined with stoical common sense, inspire us to think critically about our economic systems and the interests they serve. Readers are encouraged to peruse the “Notable Quotes” section after this introduction to experience the potency of Smith’s language on a variety of issues. *The Wealth of Nations* is a sumptuous feast of political economy. *Bon appetite.*

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