

The Concept of Abstract Labour in Adam Smith's System of Thought

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ABSTRACT *This paper draws attention to the fact that in the Wealth of Nations Smith conceptualises labour as a malleable, adaptable resource, capable of undertaking whatever may be required of it as the economy evolves over time. This conception, equivalent to Marx's 'abstract labour', differs fundamentally from the neoclassical view of the labour force as comprised of individual agents, each with a given endowment of capabilities. In Smith's analysis, the flexible character of abstract labour is essential to allow the progressive extension of division of labour in the course of economic development. It is also an essential underpinning of Smith's explanation of how 'natural balance' is maintained within the economy; this implies an understanding of equilibrium values quite different from that of the later neoclassical conception. Abstract labour is furthermore a necessary element of Smith's claim that individual agents, pursuing their own ends, promote the general interest of society, understood not in terms of the attainment of an 'optimal', utility-maximising allocation of given resources, but in terms of the promotion of capital accumulation and economic development.*

1. Introduction

Commenting on the special role that the division of labour plays in the *Wealth of Nations*, Kenneth Arrow (1979, p. 155) observes that Adam Smith's idea that people benefit by specialising in particular tasks or trades and exchanging their services or goods with each other 'has been the basis of the most significant strand in the development of economics in the ensuing two hundred years.' Arrow connects this idea to Ricardo's theory of comparative advantage according to which countries with different natural endowments benefit from trade by specialising in doing what they do best. 'The Ricardo viewpoint', he observes, 'extended from foreign trade to the domestic market, has been predominant in subsequent economic theory. Like differences in natural resources, the differences in individual talents are the basis of [specialisation] and trade.'

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Arrow notes however that this view departs from Smith's formulation in which '*people are very much alike, but they have chosen to specialise in different ways because they can do better to be a specialist*' (Arrow, 1979, p. 155; emphasis added). In other words, Smith in fact rejects the notion that the utilisation of comparative advantages of different individuals is the basis of division of labour in society. As Smith understands it, specialisation rests on something other than intrinsic differences between individuals. While Arrow did not elaborate on the matter, his observation provides the starting point of the present discussion. It will be argued that the conception of labour as 'abstract' labour, that is, as a productive resource, which is characterised not by the possession of particular abilities and skills but as flexible and adaptable as circumstances may require, occupies a fundamental place in Smith's thinking on the economic process.¹

2. The Philosopher and the Common Street Porter

It will be useful for our purpose to see how Smith came to his view of the similarity of ability and talents among different people. In the first chapter of *The Wealth of Nations*, Smith (1776) informs us that his analysis is concerned with an economy that is characterised by a fairly advanced degree of division of labour, and he identifies the division of labour as the principal cause of the wealth of nations. In the following chapter he raises the question of the 'principle which gives occasion' to this phenomenon. In every civilised society, he tells us, man stands at all times in need of the cooperation and assistance of his fellowmen. This creates conditions for the emergence of exchange.

Since exchange takes place only when people are producing different things, Smith raises the question of why one person chooses to specialise in a particular product and another in something else. The manner in which Smith proceeds to deal with this question is interesting. He writes:

In a tribe of hunters or shepherds a particular person makes bows and arrows, for example, with more readiness and dexterity than any other. He frequently exchanges them for cattle or venison with his companions, and he finds at last that he can in this manner get more cattle and venison, than if he himself went to the field to catch them. From a regard to his own interest, therefore, the making of bows and arrows grows to be his chief business, and he becomes a sort of armourer. Another excels in making the frames and covers of their little huts or moveable houses. . . . (Smith, [1776] 1976, I, pp. 27–28)

¹Marx, who christened this idea of labour as abstract labour, noted Smith's adoption of this concept. 'Implicit in [the first sentence of the *Wealth of Nations*]', Marx ([1859] 1981, p. 209) wrote, 'is the rejection of all restrictions with regard to the activity that produces wealth and an assertion of the irrelevance of the specific kinds of labour.' And in *Theories of Surplus Value*, he observes that 'Surplus value itself is wrongly conceived [by the Physiocrats] because they have false ideas of value, reducing it to the use value of the labour, not to *the labour time, to social, homogeneous labour*. . . . Adam Smith frees this from the false notion with which it was linked among the Physiocrats' (Marx, 1905–1910, p. 149, emphasis added; the same view is expressed on p. 126).

And so on. In this way different people come to 'dedicate' themselves to particular activities and we have the emergence of a community of specialist producers. Smith here seems to be leaning towards the comparative advantage view of the origins of specialisation, a view whose provenance can be traced back to Plato.² It was expressed by a contemporary of Smith in the clearest possible terms: 'Men are endued with various talents and propensities, which naturally dispose and fit them for different occupations; and are . . . under a necessity of betaking themselves to particular arts and employments, from their inability of otherwise acquiring all the necessaries they want, with ease and comfort. This creates a dependence of one man upon another, and naturally unites men into societies.'³

Despite having started out in this direction, Smith thereafter distances himself from this viewpoint and comes down firmly, though in his characteristically cautious manner, on the opposite side:

The difference of natural talents in different men is in reality much less than we are aware of; and very different genius which appears to distinguish men of different professions, when grown up to maturity, *is not upon many occasions so much the cause, as the effect of the division of labour*. The difference between the most dissimilar characters, between a philosopher and a common street porter, for example, seems to arise not so much from nature, as from habit, custom and education. . . . (Smith, [1776] 1976, I, pp. 28–29; emphasis added)

He goes on in this vein and concludes that in the absence of division of labour 'All must have had the same duties to perform, and the same work to do, and there could have been no such difference of employment as could alone give occasion to any great difference of talents' (Smith, [1776] 1976, I, p. 29). This view is repeated later ([1776] 1976, I, pp. 143–144; see also p. 265) and reinforced in Book V where, discussing the deleterious effects of division of labour within a plant, he tells his readers that the 'understandings' of men 'are necessarily formed' by the kind of work they perform ([1776] 1976, II, pp. 781–782).⁴ Thus, abilities, skills and 'understandings' are acquired through education, training and experience; they are not the result of natural endowments.

These passages show that Smith subscribed to the doctrine of the 'natural equality of all men' generally held by his Enlightenment contemporaries.⁵ But

²Plato (1953, p. 212): '... we are not all alike; there are diversities of natures among us which are adapted to different occupations . . . we must infer that all things are produced more plentifully and easily and of a better quality when one man does one thing which is natural to him. . . .'

³The passage, from Joseph Harris's *An Essay upon Money and Coins* (London, 1757), is quoted by R.H. Campbell & A.S. Skinner in an editorial footnote to the *Wealth of Nations* (Smith, [1776] 1976, I, p. 28).

⁴The idea that 'understandings' of people are formed by the material conditions of life is one that runs right through the *Wealth of Nations*. For instance, the 'indolence' and 'profusion' of landowners as a class is attributed to their 'situation' in that their revenue comes to them 'without care or cost' ([1776] 1976, I, p. 265).

⁵Thus, for instance, David Hume ([1752] 1963, p. 454): 'When we consider how nearly equal all men are in their bodily force, and even in their mental powers and faculties,

to follow Smith's general line of thinking, and, indeed even to accept it, we do not need to adopt the view that all human beings are, as it were, born with a 'clean slate', nor should we allow ourselves to be sidetracked into the nature versus nurture debate. The position adopted in this paper may be summed up as follows. Smith does not require for his analysis as strong an assumption as the one he is making here. Without departing from the essentials of Smith's argument in the *Wealth of Nations* we may allow that, although individuals may have different potentials, these differences are sufficiently small that they can be neglected for the purpose of explaining the growth of the economy in which social division of labour has come firmly to be established. In the context of a dynamic, evolving system it is appropriate to suppose that labour skills and abilities are not given and unchanging, but are acquired in response to the changing needs of the economy. Thus, to follow Smith, we can do without the 'clean slate' assumption. All that is needed is to view the economy as one in which labour skills are reproducible or labour is conceptualised in abstract terms—one, that is to say, in which the skill composition of labour supply will naturally adjust to the needs of the time.⁶

3. Rationale of Division of Labour

Smith's adoption of the concept of abstract labour raises an important question that has not received adequate attention in the literature.⁷ We know that Smith rejects the principle of innate differences; the question is: what does he put in place of this principle?

Smith's answer to this question is to be found in the chapter 'Of the Division of Labour' ([1776] 1976, I, p. i). In this chapter, using the example of a pin factory he had visited, he shows how dividing a particular process of production into its various components and assigning a particular task to a single worker improves labour productivity. He contrasts this way of doing things with a situation in which only one person attempts to perform all the distinct sequential operations by himself. In the first case, where the process has been divided up into 18 distinct sub-processes and where the operation at each sub-process is performed by distinct hands, the output per person is about 5,000 pins a day, whereas 'if they had all wrought separately and independently, and without any of them having

till cultivated by education, we must necessarily allow, that nothing but their consent could at first associate them together, and subject them to any authority.' For a survey of pre-Smithian views on abstract labour, see Prendergast (1995).

⁶It is not denied that for the investigation of a different kind of problem in a different theoretical framework it may be quite appropriate to assume that 'men are endued with various talents that dispose and fit them for different occupations.'

⁷It has been often observed that Smith departed from the Platonic view of the division of labour, and that, as in the example of the pin factory, increases in labour productivity resulting from division of labour are due not to individual differences but to a more efficient organisation of production (see, for instance, McNulty, 1975). However, the question as to what precisely Smith puts in place of the Platonic notion has not been clearly formulated, and thus not answered; nor has there been any discussion of the place that the concept of abstract labour occupies in Smith's general system of thought.

been educated to this particular business, they could not each of them made twenty, perhaps not one pin a day. . . . ' ([1776] 1976, I, p. 15).

The reasoning behind this way of thinking has been neatly summarised by Arrow. Commenting on the reasons given by Smith for increases in labour productivity as a result of division of labour, Arrow (1979, pp. 154–155) writes:

When specializing, the individual is learning only what is necessary to accomplish a task and can, so to speak, spread the overhead of learning over a much longer run. A professional, such as a physician, is rather an extreme exemplification of this. A physician essentially serves you with knowledge about diseases . . . It would be possible for a person who was willing to spend five years or more at the task to acquire this knowledge. But obviously no individual can justify five years of learning devoted solely to the prospect of self-medication. It is socially worthwhile for some individuals to specialize in health care when that education can be used to handle many thousands of cases.

We see that the rationale for division of labour lies in the phenomenon of economies of scale. What holds for the physician applies equally, though less dramatically, to the worker who is specialising in a particular sub-process in pin making.

This point of view is so fundamental to the Smithian system, that we must pursue it further. We may ask why the technique (with its 18 sub-processes) that is used to produce nearly 5,000 pins a day cannot be used to produce, with the same degree of efficiency, at, say, the scale of 1,000 pins a day. The answer is that when production is organised on a large scale it is possible to find a technique of production that is more efficient than the one that is more appropriate for a smaller scale. The larger investment associated with it can be profitable only when production is on a large scale. In the absence of economies of large-scale production the same technique would be replicated both at small and larger scales of production and there would be no advantage in increasing the division of labour, and Smith's entire argument would fail.

Although division of labour at the level of the shop floor is an essential element of the mechanism of growth, the process of development cannot be understood exclusively in terms of this factor. To get a more complete picture we have to turn to social division of labour or industrial specialisation. As in so many other cases, Smith explains an important idea by using a simple illustration ([1776] 1976, I, p. 31). In 'so desert a country as the Highlands of Scotland' population is scattered in small, isolated hamlets. Here 'every farmer must be his own butcher, baker and brewer for his own family' because markets are too small to support specialised businesses of butchers, bakers and brewers. But let us now imagine that with general development (say, as a result of improvements in communications) taking place around the region there is enlargement of markets for meat, bread and beer. In Smith's story this region will now begin to experience social division of labour. There will emerge specialist producers of meat, bread and beer. The reason for the emergence of specialisation has to do with larger markets and the possibilities they create for the adoption of techniques with greater division of labour and higher productivity—techniques that call for larger investment and that are profitable only when employed at large scales of production. That is the reason why the production of bread in one large bakery,

say, for hundred families, is cheaper as compared with production at the level of the household. The same, of course, applies to other products. Eventually, with continuing economic expansion, households will give up domestic production of these items, and purchase them from specialist producers.

To see more clearly the phenomenon envisaged here, let us extend Smith's illustration a little further. Suppose that, at an early stage of the development of this economy, there are multi-product workshops producing wooden products such as cartwheels, agricultural implements, cabinets, and so on. Markets are yet too small to support specialist producers of these items. But as the market for, say, cartwheels increases, there comes a point when the making of cartwheels splits off from general woodworking and comes to be undertaken by a specialist producer.

The reasoning behind this process of industrial differentiation has already been suggested. The specialist producer makes cartwheels at a larger scale than does the general woodworking shop (although, of course, the overall size of the latter may be larger than the former). Because cartwheel production is on a larger scale the specialised producer can use more detailed division of labour and the specialist equipment that goes with this level of specialisation as compared with the multi-product enterprise that must use general-purpose tools. The specialist producer is able to undercut the multi-product firm because higher costs associated with increased division of labour and the specialist equipment can be spread over a larger volume of output. With the expansion of markets and through the actions of profit-motivated businesses, cartwheel production will eventually become a distinct trade; and with further expansion of the market it will become further differentiated. The same argument applies to the making of agricultural implements, cabinets and other trades.

The discussion of these issues leads directly to Smith's theory of economic development (see, for instance, Young, 1928).⁸ But it is not necessary, in the present context, to go further into that. We have established that the rationale for division of labour following upon Smith's rejection of the comparative advantage principle lies in economies of large-scale production. Smith's statement about similarities between people's innate abilities is not a mere rhetorical flourish of an Enlightenment man. The idea that industrial specialisation does not derive from any inherent differences among people and that the skill composition of society evolves with the process of development is an essential aspect of Smith's thinking on the subject.

4. Natural Balance of Industry

Having laid the groundwork for his theory of economic progress in the first three chapters of the *Wealth of Nations*, Smith turns to the theory of value.

⁸In order to emphasise the role of social division of labour (and, what he calls, 'more roundabout methods of production') in the process of development, Young (1928, p. 531), wrongly underplays the importance of economies of large-scale production. The latter phenomenon is central to Smith's view of social division of labour, and not merely 'an incident in the general process by which increasing returns are secured ...'

In Book I, Chapter I (pp. 22–23), Smith had drawn attention to a crucial feature of the phenomenon of social division of labour. He asked his readers to imagine the making of a simple product, the coat of an ordinary labourer, to show that, through direct and indirect industrial linkages, practically all the branches of the economy contributed to the manufacture of this item. More generally, Smith conceives of the economy as a system in which every branch of production depends, directly or indirectly, on others for its inputs and therefore its operations. All industries are bound together in a network of quantitative relationships. There is a ‘natural connection of all trades’.⁹

Economic development is associated with increasing social division of labour. In a dynamic economy trades differentiate, they multiply in numbers, new industries emerge, old ones decline or disappear, capital accumulates and is reallocated across industries. In other words, there is constant disturbance of the ‘natural connection of all trades’. These disturbances take the form of overproduction of some commodities and underproduction of others. Such imbalances, if they remain uncorrected, would result in the system’s breakdown. Economic development therefore requires a mechanism that restores the ‘natural connection of all trades’. The purpose of the theory of value for Smith is to establish the presence of tendencies in the economy that help correct the imbalances that inevitably arise in the course of economic progress.

Thus, the theory of value or, what comes to the same thing, the theory of natural balance (static analysis) and the theory of development (dynamic analysis) do not, in Smith’s system, stand in opposition to each other. Smith’s analysis of the division of labour necessarily leads him toward a realisation of the need for a coordinating mechanism that would tend to restore the balance of an economy in a process of change.¹⁰

The thesis of this paper is that the notion of abstract labour has a central place in the balancing mechanism devised by Smith. The central idea of the theory of the natural balance is to be found in Smith’s discussion of the theory of value in the case where labour is the only productive resource. We will consider this case in some detail as the reasoning developed in the labour-only case extends easily to the more general situation in which capital is also brought into consideration.

Smith opens his discussion of the theory of value with his famous example of the beaver and deer hunters. In ‘that early and rude state of society which precedes both the accumulation of stock and appropriation of land’, the labour-quantity principle is the only rule that can provide the basis of exchange. If it costs

⁹This is one of Smith’s fundamental points. Different sectors of the economy are ‘essentially necessary either to the existence or extension of’ each other and ‘to the general conveniency of the society’ ([1776] 1976, I, p. 360). We can see Smith here suggesting an organic view of the economy.

¹⁰Kaldor (1972, pp. 1240–1241) has argued that ‘economic theory went astray’ when the ‘theory of value took over the centre stage’. This happened (according to Kaldor) when Adam Smith, after having presented a brilliant account of the process of division of labour, was sidetracked into value (equilibrium) theory. The present discussion is partly intended as a rebuttal of Kaldor’s contention.

twice the labour to kill a beaver than it does to kill a deer, one beaver should ‘naturally’ exchange for two deer ([1776] 1976, I, p. 65).

It is ‘natural’ that the exchange ratio between the two products should always be determined by their costs of production (in terms of labour) because labour of the same kind—‘common labour’—is the only productive resource here. In this situation, if, say, there is overproduction of deer and underproduction of beaver, the actual exchange ratio between the two products (their market prices) will diverge from the natural ratio (their natural prices), and the real hourly earnings of beaver hunters, in terms of either of the two goods, will be higher than those of the deer hunters.¹¹ Divergence between the earnings of hunters having the same ability with respect to hunting both the animals indicates a state of imbalance. Given that every person wishes to improve his or her position and that the principle of ‘perfect liberty’ prevails (that is, there are no institutional barriers to the mobility of resources between different lines of production) this differential between earnings will induce some of the deer hunters to take to beaver hunting; as a result more beavers and fewer deer will be produced. This in turn will initiate a tendency for the market exchange rate to move toward the natural rate, and for earnings in the two activities to be equalised. When the actual exchange rate comes to coincide with the natural rate, and the hourly earnings of hunters in both the activities are equal the system will be in a state of balance.

The result that there is a persistent tendency for one beaver to exchange for two deer depends crucially on the assumption that competition prevails (labour can move freely between the two activities), and on the further assumption of homogeneous labour. Relative prices here are determined ‘objectively’, that is, by physical (labour-time) costs and without reference to consumers’ subjective preferences. This result is usually attributed to the fact that we have here only one ‘scarce’ factor of production. As Schumpeter (1954, p. 310) puts it, ‘in this special case (where labour is all of the same quality), all theories of value would arrive at the same result’.

Having considered this situation, Smith moves on to the case where there is labour of different types, with acquired skills of different degrees of ‘dexterity and ingenuity’:

[I]f the one species of labour requires an uncommon degree of dexterity and ingenuity, the esteem which men have for such talents, will naturally give a value to their produce, superior to what would be due to the time employed about it. Such talents can seldom be acquired but in consequence of long application, and the superior value of their produce may frequently be no more than a reasonable compensation for the time and labour which must be spent in acquiring them. In the advanced state of society allowances of this kind, for superior hardship and superior skill, are commonly made in the

¹¹Smith defines natural price as one governed by costs, without reference to subjective factors. The market price is the price at which a commodity is actually sold; it is affected by current demand relative to the amount brought to the market. The subjective element dominates here ([1776] 1976, I, pp. 72–74).

wages of labour, and something of the same kind must probably have taken place in its earliest and rudest period. (Smith, [1776] 1976, I, p. 65)

The same idea is expressed in a later chapter ([1776] 1976, I, p. 118) where Smith likens the acquisition of a skill to the 'erection of an expensive machine'.

The principle of natural balance (natural values determined by costs, measured in homogeneous labour, and equality of earnings) that is suggested for the simple, 'one-factor' case holds also when we have labour with different types of acquired skills. The quantity of labour used in the production of a commodity now is seen as direct as well as indirect (common labour embodied in, or invested in the acquisition of, the skill), and Smith gives us an unambiguous conversion factor ('time and labour which must be spent in acquiring' the relevant skill) to conceptually reduce indirect to common, homogeneous or, what is the same thing, abstract labour. With labour of different degrees of 'dexterity and ingenuity' thus made theoretically commensurable, we can compare different types of labour embodied in different commodities by the same standard—units of 'common labour'.

The difference between the two situations, of course, is that while in the first case labour is factually homogeneous, in the second, homogeneity exists only as a potentiality (we might say, as an abstraction). In the first case, since the labour of the same type moves from one activity to the other, the process of adjustment, or the restoration of the natural balance, is fairly simple and apparent. In the second case, when there is a state of imbalance in the system, hunters, the demand for whose product has declined, must learn the new skills, the demand for whose product has increased. The process of adjustment here is less straightforward and transparent and, in practice, faces greater obstacles than in the first case. Smith is aware of the difficulties of such adjustments in real life; he discusses them in Chapters vii and viii. But he insists that when the principle of 'perfect liberty' prevails there is a persistent tendency in the system to move it toward its state of natural balance ([1776] 1976, I, p. 75).

Although the principle of 'perfect liberty' is essential for the system to achieve its natural balance, that is not enough. The skills of labour must be fully adaptable to the changing needs of the economy. Again we make the point that, to model the equilibrating process, labour must be conceptualised as abstract or potentially homogeneous. In both cases the natural balance of the system is determined on the same principle, and in both cases natural values are determined 'objectively' (in terms of homogeneous labour), without reference to the subjective preferences of consumers. While, in the first case, all theories of value would arrive at the same result, in the second they will not. The assumption of homogeneity of labour implies a particular view of the nature of equilibrium relative values and, also, a corresponding theory of value significantly different from that which derives from the Platonic approach, which underlies the neoclassical theory.

It is instructive to contrast Smith's thinking on the subject with the Platonic case, where differences between different types of labour are innate or given in their technical characteristics. Here, allocation of different types of labour—distinct factors of production—to different activities will take place on the basis

of their innate comparative advantages. The labour-quantity principle obviously has no place in this model. In this case, no conversion factor is available that will make different types of labour commensurable. Hence, natural values and the relative earnings of hunters cannot be determined without reference to the relative scarcity of different types of skill advantages that hunters possess; the latter, in turn, will depend on the available endowment of these skills and on consumers' preferences for their products. Natural prices and earnings of hunters will reflect such relative scarcities. Thinking along Platonic lines necessarily leads to this result.

By contrast, in the Smithian system, equilibrium values are not indices of scarcity. Here, relative scarcity exists only as a reflection of an imbalance in the system when the market price diverges from the natural price, a temporary phenomenon that is eventually corrected by labour adapting its skills in response to changes in the production system. Thus, for example, if the market price of beaver exceeds its natural price and earnings of beaver hunters (taking direct and indirect labour into account) exceed those of deer hunters, some of the deer hunters will acquire the beaver hunting skill, thus setting into motion the tendency for market prices to coincide with natural prices and earnings in the two activities to be equalised. The relative scarcity of beaver hunters will disappear and natural prices will again reflect costs measured objectively in terms of labour hours. The notion of abstract labour—labour that can adapt itself to produce any commodity with equal facility—and the phenomenon of relative scarcity—a concept founded on the Platonic notion of resources being fixed in their technical characteristics—are mutually exclusive.

After considering the labour-only situation, Smith moves on to the 'advanced state of society' and now has to take account of the fact that there are two other resources, land and capital. Smith surmises that in the 'improved society' there must therefore be three components of cost and value, as there must be three distributive shares ([1776] 1976, I, pp. 67–69). This part of Smith's discussion has been interpreted to suggest that he regards each component of cost as independent of the others, so that as one component changes, the value of the good always changes in the same direction.¹²

There are other passages in the *Wealth of Nations* where it seems that Smith has not given up on the labour-quantity principle ([1776] 1976, I, pp. 67, 87).¹³ Both Marx and Schumpeter subscribe to this view. According to Marx (1905–1910, p. 113), whenever Smith is considering the phenomenon of 'surplus value in general' he reverts to the labour theory of value. Schumpeter (1954, pp. 309,

¹²See Sraffa (1951, Section IV) for a discussion of Ricardo's objections to this 'adding up' theory. But in his chapter 'Of the Rent of Land', Smith takes a position on rent that is inconsistent with 'adding up' reasoning: 'Rent', he writes, 'enters into the composition of the price of commodities in a different way from wages and profit. High or low wages and profit, are the causes of high or low price; high or low rent is the effect of it' ([1776] 1976, I, p. 162).

¹³See also his discussion, in Chapter xi, of how increases in the division of labour and the introduction of machinery affect prices.

188–189) maintains that, in addition to his ‘three components’ cost of production theory he also subscribes to the labour theory of value (perhaps to more than one labour theory of value).

There can be little doubt that there are ambiguities in Smith’s treatment of value under conditions of capitalist production; and that there are difficulties with both the ‘three components’ theory and the labour theory of value. But, equally, there can be no doubt that these difficulties do not affect his thinking on the subject of the natural balance. He adheres to the position that prices are determined by costs; and there is no ambiguity in his definition of natural price, which is determined before the commodity is brought to the market. Capital, like labour, is conceived as malleable so that with sufficient time for adjustment it can, like labour, take the shape that is required by the production system (recall that he likens the acquisition of a skill to the ‘erection of an expensive machine’). As we saw earlier, in the labour-only case the process that restores natural balance is grounded in labour mobility and the adaptability of labour’s skill composition. Now, in addition, this process incorporates mobility of capital and the reshaping of the composition of the capital stock. The latter process takes place through the wearing out or discarding of obsolete machines and their replacement by machines that better fit the requirements of the production system. The condition for the system to be in its state of ‘repose and continuance’ ([1776] 1976, I, p. 75) is the tendency for wages and the rate of profit to be equalised across all branches of the economy. This tendency becomes effective only if there is free movement of resources and if labour and capital are conceptualised as malleable, or abstract.

To summarise: we have shown that Smith’s theory of value—his static analysis—arose from the need to work out a coordinating mechanism that would ensure that an evolving economy would maintain its balance without any external intervention. The price mechanism thus devised is intended to serve Smith’s analysis of the development process—his dynamic analysis. The basic presumption is that labour, and resources in general, adapt qualitatively to changing division of labour. The concept of adaptable or abstract labour is thus fundamental both to how productivity increases through specialisation and to how the internal balance is maintained in an evolving economic system. Given the objective of his inquiry, Smith could not have adopted the Platonic outlook, because an economy conceptualised in that way could have no internal source of change: ‘if [such a system] changes at all it does so under the influence of events which are external to itself’ (Schumpeter, 1951, p. 159).

This understanding of Smith’s thinking suggests an interpretation of his famous observation that the individual while pursuing his own self-interest is led as if by an invisible hand to promote the general interest of society ([1776] 1976, I, p. 456) that is different from the conventional reading. This alternative interpretation is free of any subjectivist elements that, as we have seen, are excluded by the assumption of abstract labour and thus have no place in his system of thought.

5. The General Interest of Society

It is often suggested that Smith’s statement concerning the correspondence between the pursuit of self-interest and the general interest of society is grounded

in the same reasoning that underpins the fundamental propositions of neoclassical economic theory.¹⁴ In this theory the focus is on the final consumer. Society's resources are owned by individuals or households, who have certain psychological preferences in relation to the goods they wish to consume. Businesses borrow or buy from households these resources and transform them into consumer goods. The outcome of the market process—firms hiring resources from households and then selling to consumers the goods they desire—is considered as socially optimal. In this situation, every individual in society, given his wealth and tastes, is maximising his utility; and one person's wellbeing can be increased only at the cost of some one else's. This is the ideal of efficiency that the invisible hand achieves, the socially optimal allocation of given resources. This reasoning is extended to the process of accumulation, which is seen as a manifestation of individuals' choice between present consumption and future consumption.

But this approach is completely alien to Smith's way of thinking. The concept of consumer preferences as it appears in neoclassical economics has no place in his system of thought. Smith disapproves of luxury consumption. In fact, he disapproves of all 'unproductive' consumption—consumption that does not contribute to the generation of investable surplus. He declares the 'prodigal' a 'public enemy'. 'By not confining his expense within his income, he encroaches upon his capital'; he is like someone 'who perverts the revenue of some pious foundation to profane purposes'. The frugal person, by contrast, is like someone who 'establishes, as it were, a perpetual fund' for the employment of productive labour ([1776] 1976, I, pp. 338–340). Smith's utter disdain for landowners as a class rests on his view that they are given to 'profusion' and 'prodigality'. He speaks scornfully of their love of 'trinkets' and 'baubles' ([1776] 1976, I, p. 421). And he notes ([1776] 1976, I, p. 265) that this behaviour arises from the historical development of the landowning class and that landowners 'are the only one of the three orders [of society] whose revenue costs them neither labour nor care, but comes to them, as it were, of its own accord'.¹⁵

Smith's suggestion regarding the harmony of private and public interest is advanced first in Book II, which deals with capital accumulation, and then in Book IV, which is largely devoted to a critique of the 'mercantile system', a discussion that is set in the context of economic development.¹⁶

¹⁴Kaldor (1972, pp. 1240–1241) sees a continuous line of theoretical development running from Smith through Ricardo, Walras, Marshall 'right up to Debreu ...' In the same vein, Samuelson (1992, p. 5) writes: 'Given their respective dates we might better compliment Walras for his Smith-like approach to general equilibrium.' According to Schumpeter (1954, pp.189, 472), Chapter vii of the *Wealth of Nations* points in the direction of Walras.

¹⁵Rostow (1992, p. 40) comments that 'Smith, in passages such as these, which apparently reject the ultimate legitimacy of consumer's sovereignty, is writing as a moralist at least as much as a market analyst.'

¹⁶The context in which this statement is made is worth noting. On the conventional view this statement should occur in Chapter vii (which, as noted earlier, Schumpeter sees as pointing in the direction of Walras). Thus, Maurice Allais (1992, p. 32) finds the placing of this statement in Book IV as due to Smith's faulty exposition.

Smith opens his discussion of capital accumulation (Book II) by observing that the extent of division of labour, the principal factor in the process of development, depends on the previous accumulation of capital:

As the accumulation of stock must, in the nature of things, be previous to the division of labour, so labour can be more and more subdivided in proportion only as stock is previously more and more accumulated. . . . As the accumulation of stock is previously necessary for carrying on this great improvement in the productive powers of labour, so that accumulation naturally leads to this improvement. ([1776] 1976, I, p. 277)

Thus, capital accumulation for Smith becomes a central factor in the development of the economy. It is in this context that he censures the profligate (and the waste and extravagance of governments) and commends the frugal. And it is here that he introduces the idea that it is natural to man to seek to improve his condition and that this desire should result in the promotion of public good ([1776] 1976, I, pp. 342–343). The natural desire of every individual to better his condition is manifested in frugality and savings that contribute to capital accumulation. It is in this manner that while seeking to enrich himself, the individual also contributes to economic progress, which Smith associates with the general interest of society.

Smith returns to the idea of the harmony of private and public interest in Book IV where, in the course of his attack on the mercantile system, he elaborates his concept of the natural balance of the economy. His main indictment against this system is that its policies ‘derange’ the natural balance of the economy and are therefore inimical to progress:

Every derangement of the natural distribution of stock is necessarily hurtful to society in which it takes place; whether it be by repelling from a particular trade the stock that would otherwise go to it, or by attracting towards a particular trade that which would not otherwise come to it. (Smith, [1776] 1976, II, pp. 632–633)

Herein lies the main rationale of the principle of natural liberty. Under its rule, profit-motivated business will be free to employ their capital where profits are higher than the normal rate, that is, where there is underproduction; and they will be able to withdraw capital from those sectors of the industry where there is overproduction and profits are below the normal rate. By restoring in this way the correct distribution of stock in the economy, the pursuit of private interest promotes the ‘progress of society towards real wealth and greatness’ ([1776] 1976, II, p. 687). Hence,

Without any intervention of law, therefore, the private interests and passions of men naturally lead them to divide and distribute the stock of every society, among all the different employments carried on in it, as nearly as possible in the proportion which is most agreeable to the interests of the whole society. ([1776] 1976, II, p. 630; see also I, pp. 455–456)

The important supposition here is that, generally (though not necessarily in every case), under competitive conditions a profit rate higher than the normal rate indicates a higher—and a profit rate lower than the normal rate a lower—social priority in the sense that it promotes economic progress. Thus, when profit-motivated businesses respond to market signals by undertaking new investments

in the former and withdrawing capital from the latter, they are performing a socially beneficial purpose.

The upshot is that when considering the subject of the harmony of private and public interests, the individual as consumer with given preferences never enters Smith's thinking: it is the individual as a contributor to accumulation and economic progress that he has in mind.

According to Smith, then, the pursuit of self-interest in a framework of appropriate institutions leads to increasing national wealth. But on what grounds can we equate an increase in national wealth with the 'general interest' of society? Indeed, what do we mean by the 'general interest' of society?

In Smith's way of thinking, the 'general interest' of society is understood entirely in terms of 'universal opulence' or the general prosperity of the population. And the index of general prosperity is the wage rate, per capita income of the vast majority of the population: 'The liberal reward of labour, . . . as it is the necessary effect, so it is the natural symptom of increasing national wealth' ([1776] 1976, I, p. 91). And (I, p. 95):

Servants, labourers, and workmen of different kinds, make up by far the greater part of every great political society. But what improves the circumstances of the greater part can never be regarded as an inconveniency to the whole. No society can surely be flourishing and happy, of which the greater part of the members are poor and miserable.

Further, it is not great national wealth, but its sustained increase over time that generates general prosperity and the rising incomes of the working people. The justification for the system of natural liberty is therefore to be found in increasing national wealth over time:

It deserves to be remarked, perhaps, that it is in the progressive state, while the society is advancing to the further acquisition, rather than when it has acquired the full complement of riches, that the condition of the labouring poor, of the great body of the people, seems to be the happiest and the most comfortable. It is hard in the stationary, and miserable in the declining state. The progressive state is in reality the cheerful and hearty state to all the different orders of society. The stationary is dull; the declining, melancholy. (Smith, [1776] 1976, I, p. 99)

Here, Smith's reasoning seems to be as follows: if capital accumulation and economic growth slow down, even at a high level of development, demand for labour will slacken. But the supply of labour will continue to increase as long as the wage rate is above the subsistence level.¹⁷ Eventually, with continuing slow-down in the rate of accumulation, the supply of labour will catch up with the demand for labour at

¹⁷The subsistence wage in Smith is made up of two components. First, labour is an input as, for instance, are farm animals. Workers must be fed for the economy to reproduce itself. There is therefore a minimum threshold below which the wage rate cannot fall if the economy is to remain viable. The other component is socially determined; the wage rate must conform to prevailing notions of 'common humanity' ([1776] 1976, I, p. 86). The size of this component is a product of economic, political and social development. With economic growth it rises over time, but it can also fall if economic conditions

the subsistence wage. When this situation materialises, we have the stationary state when 'things are at a stand' and when the 'labouring poor' receive no more than their 'scanty maintenance' or bare subsistence ([1776] 1976, I, p. 91). But when capital is accumulating and national wealth is increasing, demand for labour keeps ahead of supply. In these conditions, competition among employers for labour undermines their combinations to keep wages low and the bargaining position of labour is strengthened. Thus, a buoyant market for labour ensures that the wage keeps rising.

Smith's analysis of the long-run behaviour of wages has been subject of much debate (see, for example, Dobb, 1973). However, the argument of this section does not depend on the completeness of Smith's theory of income distribution. The point that we have tried to make in this section is that in Smith's scheme of thought the proposition regarding the harmony between private interest and the interest of society is entirely free of any subjectivist considerations; and that this proposition makes sense only in the context of his principal theoretical and policy concern—the increase over time of the wealth of the nation, which, pragmatically, he equates with the general interest of society. This is, of course, the same concern that necessitated his treatment of labour as abstract labour.

6. Conclusion

We have argued that the assumption of abstract labour by Smith is dictated by his choice of the kind of economy he is studying—a capitalist economy characterised by a fairly advanced degree of social division of labour—and by the nature of the problem he is investigating—causes of increase in the wealth of nations. It was natural for him to conceptualise labour as adaptable to changing circumstances, rather than as an entity with fixed technical characteristics, for he saw the development process in terms of advancing social division of labour, which entails the creation of new industries, skills and other resources to suit the requirements of the time. The alternative assumption of concrete labour would have left no room for the principle of objective historical change, a principle on which Smith's mind was focused. This interpretation of Smith's thinking points toward a reading of the famous statement about the role of the invisible hand that is very different from that usually attributed to him.

Acknowledgments

I am grateful to Roy Grieve for his valuable comments on the first draft of this paper. I am also indebted to two referees of this journal for their helpful suggestions.

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deteriorate. The notion that a crucial economic variable such as the natural wage rate is influenced by political, cultural and social factors is fundamental to Smith's thinking.

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