

The Other Revolution of '76

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IN 1976 WE WILL celebrate the bicentennial year of the American Revolution and our founding as a free nation, with toasts and hosannahs for the signers of the Declaration of Independence and the framers of the Constitution. But if 1776 was the watershed year for the political life of America, so was it also the watershed year for the economic life of America. For in 1776, between the appearance of Thomas Paine's *Common Sense* in January and the Declaration in July, *An Inquiry into the Nature and Causes of the Wealth of Nations* by Adam Smith was published. A most remarkable book. This one book reconstituted the industrial revolution and launched the capitalist revolution, at least intellectually. Walter Bagehot said that because of this one book "the life of almost everyone in England—perhaps of everyone—is different and better. . ."¹ William Pitt in introducing the budget to Parliament in 1792, echoed Edmund Burke and said this one book furnishes "the best solution to every question connected with the history of commerce, or with the systems of political economy."² Henry Thomas Buckle in his *History of Civilization in England* said:

This solitary Scotchman has by the publication of one single work, contributed more to the happiness of man than has been effected by the united abilities of all the statesmen and legislators of whom history has presented an authentic record.³

Be that as it may, the two revolutions of 1776—American and capitalist—were more than coincidence. Both represented reactions against mercantilism, a system of political economy characterized by aggressive nationalism, central direction and closed economies. Both represented grand endeavors to advance the cause of a free society through the establishment of limited government, although one was mainly political in scope while the other was mainly economic. Both sought, each in its own way, a system of checks and balances, of separation of powers, of freeing the individual—with the ultimate sovereignty of the one residing in the citizen, and with the ultimate sovereignty of the other residing in the consumer. In this article, some of the origins and implications of the capitalist revolution on both sides of the Atlantic are

examined, with Smith's *Wealth of Nations* as a guide.

To be sure, notwithstanding popular mythology and still another extraordinary coincidence in Smith's given name, Adam Smith was not strictly the father of political economy nor the sole pathfinder to the capitalist revolution. Smith stood on the shoulders of Enlightenment philosophers such as Locke, Berkeley, Mandeville, Hutcheson, and Hume and of Physiocrat thinkers such as Cantillon, Gournay, Turgot, Quesnay, and Rivière. John Locke and other Enlightenment writers stressed the security of private property and the insecurity of unlimited government. Mercier de la Rivière opposed the royal maxim of "l'Etat, c'est moi" and stressed "l'ordre naturel" in which the particular interest of the individual would not diverge from the general interest of a free society; Jean Vincent de Gournay is credited with coining the phrase "laissez faire, laissez passer." These ideas were not only reflected in the thinking of Smith; they also found expression in the reasoning of the Founding Fathers, from the Declaration to the Bill of Rights. (The Fifth Amendment, for example, carries verbatim Locke's phrase of "life, liberty, or property," which is of course paraphrased in the Declaration as "life, liberty, and the pursuit of happiness.") Thus the genius of Adam Smith was to reach back to the limited government ideas of the Magna Charta and the Petition of Right, to synthesize the best of the Enlightenment and Physiocrat writers, to deliver a fatal blow against the doctrine of mercantilism and to demonstrate that a free society and a free economy were inseparable—that one could not exist without the other.

The grand design of mercantilist theory and practice was, in one way or another, nationalist and bullionist; it aimed at accumulation of national "treasure," mean-

ing precious coins and bullion—gold and silver. To this end, colonies were sought, with sovereign and merchants aiding and abetting each other, as can be seen in the chartering in 1600 of the East India Company (the very same company whose tea was dumped in Boston Harbor more than a century and a half later). Colonialization meant more land, more people, more production, more taxes—more "treasure." Colonialization meant discovery and conquest, sometimes ruthlessly, as with the American Indians. Mercantilism also involved colonial production of as great a supply of raw materials as possible; the idea was that the mother country would manufacture them into finished goods, with the colonies as a prime and captive market and with a good net profit accruing to the mercantilist nation.

Another key mercantilist precept held that the nation should seek a "favorable" balance of trade—exports exceeding imports, with the difference made up by bullion; conversely, it should avoid like a plague an "unfavorable" balance of trade—imports exceeding exports, with the difference leading to a loss of bullion. Accordingly, government domestic and foreign economic policy would be vigorous and most interventionist—replete with restrictions, regulations, prohibitions, exemptions, licenses, navigation laws, labor laws, bounties for exports, and tariffs against imports. Usury laws controlled interest rates. Sumptuary laws controlled "conspicuous consumption." Corn laws sought to make the nation self-sufficient in food—no matter what the cost. Louis XIV's Minister Colbert practiced mercantilism to a "T," according to Dunoyer who tells us:

. . . the state exercised over manufacturing industry the most unlimited and arbitrary jurisdiction. It disposed with-

out scruple of the resources of manufacturers; it decided who should be allowed to work, what things they should be permitted to make, what materials should be employed, what processes followed. . . . Not the taste of the consumer, but the commands of the law must be attended to. . . . Machines were broken, products were burned, when not conformable to the rules. . . . An artisan could neither choose the place in which to establish himself nor work at all seasons, nor work for all customers. There exists a decree of March 30, 1700 which limits to eighteen towns the number of places where stockings might be woven. A decree of June 18, 1723 enjoins the manufacturers at Rouen to suspend their works from the 1st of July to the 15th of September, in order to facilitate the harvest. Louis XIV, when he intended to construct the colonnade of the Louvre, forbade all private persons to employ workmen without his permission, under penalty of 10,000 livres, and forbade workmen to work for private persons, on pain for the first offense of imprisonment and for the second of the galleys.⁴

By 1776 England's colonies stretched from America to Australia. For colonial America English mercantilist policies were manifest in such laws by Parliament as the Trade Acts, the Navigation Acts, the Stamp Act (which led to the Stamp Act Congress), the Sugar Act, the Townshend Acts, the Molasses Act, the Tea Act, and the Staple Act. Consider the Navigation Acts passed initially in 1660; then Parliament ruled that "foreign" ships and merchants were precluded from trade with the colonies, and major enumerated commodities, such as tobacco, were to be exported only to England or English possessions, even if ultimately destined elsewhere. Or consider the Staple Act of 1663; then Parliament sought to further protect British merchants and

augment British treasure by requiring commodities from European countries destined for British colonies to be shipped "triangularly" via English ports and merchants. Or take the Molasses Act of 1733; then Parliament yielded to British West Indies planter interests and sought to outlaw colonial trade with the non-British parts of the West Indies by imposing import duties on "foreign" sugar, molasses and rum. But British customs officials in the colonies were venal; British naval patrols—because of England's many wars during the eighteenth century—were inadequate to police smuggling; and, accordingly, illicit trade with the foreign West Indies became something of a cornerstone of northern colonial merchant commerce.⁵ Again, to protect British manufacturers Parliament forbade Americans to ship wool, woolens and hats from one colony to another on pain of seizure of shipments. Similarly, in 1750 Parliament prohibited American iron producers from putting up slitting and plating mills; the law required colonial ironmongers to ship their iron to Britain to be slitted and plated and then returned to America as finished products. Complained Benjamin Franklin:

Britain would, if she could, manufacture and trade for all the World;—England for all Britain;—London for all England;—and every Londoner for all London.⁶

So under mercantilism the state controlled practically every phase of economic activity—with a view toward the accumulation of bullion, the maintenance of low wages, the self-sufficiency of agriculture, the maximization of manufacturing, the attainment of an export surplus, the fixing of low interest rates, and so on. In addition, the state called for a powerful army and navy, colonies anywhere and everywhere, a big population with a growing

labor force, and intense rivalry with other nations, with the consequence of frequent wars.

Into this mercantilist milieu came that remarkable Scot, Adam Smith. Smith was born in the village of Kirkcaldy in 1723. At the age of 14 he matriculated at the University of Glasgow. There he came under the tutelage of Francis Hutcheson, a teacher who professed a utilitarian conviction in "the greatest happiness for the greatest number" as a rule of political economy—a rule Smith embraced wholeheartedly. Smith later became professor of moral philosophy at the University of Glasgow, and in 1759 published his *Theory of Moral Sentiments*—a work putting forth the moral case for individual prudence, justice, and benevolence and hence for a free society, and a work that was clearly a harbinger of his *Wealth of Nations*. He spent the years from 1764 to 1767 in France as a tutor to the young Duke of Buccleuch. In France he met with the leading French intellectuals, including, apart from the Physiocrats, Voltaire, Diderot, Helvetius, and d'Alibert. After the publication of the *Wealth of Nations*, he became commissioner of customs for Scotland in 1778 and lord rector of the University of Glasgow in 1787. He died in 1790.

At the heart of *Wealth of Nations* is Smith's understanding of human nature and incentives. To Smith self-interest could and would be harnessed to the social interest, as long as each man "does not violate the laws of justice." Hence both community and national interest could best be furthered by leaving

every man . . . perfectly free to pursue his own interest in his own way and to bring both his industry and capital into competition with those of every other man, or order of men. . . . It is not from the benevolence of the butcher, the brewer, or the baker, that

we expect our dinner, but from their 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.⁷

Self-interest would lead naturally to specialization, to what Smith called division of labor. He supplied a graphic illustration of pin-making to evidence the increased productivity under division of labor. He noted that an ordinary workman might perhaps be able to make one pin a day "and certainly could not make twenty," assuming he had neither the equipment of the day nor the experience of pin-making. But productivity would boom by building the specialized skills, dexterities and judgments of workmen up and breaking the pin-production process down, breaking it down into as many as

eighteen distinct operations, which in some manufactories, are all performed by distinct hands. . . . I have seen a small manufactory of this kind where ten men only were employed . . . make among them upwards of forty-eight thousand pins a day.⁸

Thus to Smith the problem of maximizing production, trade and "the wealth of nations" was mainly a problem of giving free rein to the innate propensity of man to division of labor and to "truck, barter and exchange one thing for another."⁹ Free trade, then, was also a key to the "wealth of nations." And while Smith ranged over the intricacies of theory and practice on money, commodities, land, labor, taxes, prices, agriculture and colonies, it is free trade and its implications with which he was mainly concerned. On land, for example, he thought little of the law of primogeniture, under which the first son was the sole heir. Accordingly, he advocated free trade of land, and asked for

repeal of statutes requiring primogeniture, entails and other constraints on the free transfer of land by sale, gift or devise.

On colonies, to cite another example, he argued that protective monopolies and triangular trade imposed on colonial commerce violated the colonists' "natural rights." With particular reference to the question of how to deal with rebellious American colonists, Smith proposed union rather than division, a common market rather than a divided market, free enterprise rather than Crown monopolies. He argued that American colonists were certainly entitled to representation in Parliament, with representation proportional to tax revenues. Indeed, if colonial contributions to the royal treasury were to exceed those generated by local taxes, the capital might even be shifted from London across the Atlantic "to that part of the Empire which contributed most to the general defence and support of the whole."¹⁰ And if the friction between America and the mother country could not be removed amicably, he advocated American independence, even though he doubted—correctly, it turned out—that England would ever voluntarily give up her authority over her colonies.

On trade itself, Smith sailed right into the heart of mercantilist doctrine when he pushed for free trade and attacked the doctrine of a so-called "favorable" balance of trade along with its system of regulations, prohibitions, export bounties, import duties, and trading monopolies. He held national and regional economic development stems from the volume and freedom of trade, internal and external, rather than from the inflow of bullion, so worshipped by mercantilist writers and practitioners, notwithstanding the fact that inflow of vast bullion from the New World had inflicted a cruel price inflation on the Old World, and especially on Spain. Free trade is the

key to the "wealth of nations," said Smith, adding that "wealth does not consist in money, or in gold and silver, but in what money purchases, and is valuable only for purchasing."¹¹

Further, Smith argued that territorial division of labor is as advantageous and natural as is occupational division of labor. Wine, for example, need not necessarily be imported from Spain. Grapes could be grown in hot houses in Scotland and presumably the profit on wine could be retained by the British. But wine production in Scotland made little sense to the canny Scotsman, noting that the English would be the poorer for it because of the higher costs and smaller market under a system of protection of domestic wine; moreover, by not buying Spanish wine, the British impeded the Spanish from buying English wares, such as textiles, in which the British had a comparative advantage—as David Ricardo was also to demonstrate later. Smith caps the argument with one of the most famous statements in economic literature:

It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy. The taylor does not attempt to make his own shoes, but buys them of the shoemaker. The shoemaker does not attempt to make his own clothes, but employs a taylor. The farmer attempts to make neither the one nor the other, but employs those different artificers. All of them find it for their interest to employ their whole industry in a way in which they have some advantage over their neighbours, and to purchase with a part of its produce, or what is the same thing, with the price of a part of it, whatever else they have occasion for. What is prudence in the conduct of every private family, can scarce be folly in that of a great kingdom.¹²

However, Smith was not the most pure of free traders and provided for two broad exemptions from the free trade rule. He maintained that domestic industries crucial to the defense of the country—such as shipping to Britain at that time—might be fit candidates for protection, since “defence . . . is of much more importance than opulence.”¹³ And he maintained that when a tax is levied on certain domestic goods an equal tariff might be levied on imported goods of the same type. He also believed that tariffs should be leveled down “slowly, gradually, and after a very long warning,”¹⁴ so that investors could extricate their capital and workers shift to new jobs.

Workers received special care and sentiment in the *Wealth of Nations*. Smith railed against legal sanctions against free wage rates and trade unions. In like manner, Smith attacked the anti-worker apprenticeship and settlements statutes emanating from the Elizabethan era, statutes that the mercantilists readily embraced. He observed that the law of apprenticeship stipulated that no person work in any trade or craft unless he had apprenticed for seven years at least. Smith argued that such long apprenticeships, under which masters were obligated to furnish only subsistence, were as perverse as they were unnecessary. They restricted the supply of labor, making goods scarcer and costlier. They bred indolence and exploitation, holding workers in a virtual state of bondage. In certain common mechanic trades, he held that only a few days training were necessary before a young man could be advanced to a journeyman; in many other trades but a few weeks were necessary. Seven years of apprenticeship, on the other hand, denied incentives, incurred frustration and constituted a crass violation of the worker’s natural rights. These rights included contracting for his services with the highest bidder, freely

choosing his craft, moving to another town or even to another country in order to better his condition, and shifting to a better-paying occupation or position. Here Smith borrowed from Locke’s ideas, stating:

The property which every man has in his own labour, as it is the original foundation of all other property, so it is the most sacred and inviolable. The patrimony of a poor man lies in the strength and dexterity of his hands; and to hinder him from employing his strength and dexterity in what manner he thinks proper without injury to his neighbor, is a plain violation of this most sacred property. It is a manifest encroachment upon the just liberty both of the workman, and of those who might be disposed to employ him.¹⁵

Similarly the Elizabethan statute on settlements, a poor law which long foreshadowed the current if not eternal controversy over welfare, was obnoxious to Smith. The law provided that every parish had to provide for its own poor. The upshot was to greatly impede the mobility of labor. The law thereby worked special hardships on ambitious apprentices and unskilled workers. It caused a scarcity of hands in one parish and a super-abundance in another. It led to onerous poor taxes in some parishes and distorted the efficient allocation of resources for the entire economy. Concluded Smith in a compassionate vein:

There is scarce a poor man in England of forty years of age, I will venture to say, who has not in some part of his life felt himself most cruelly oppressed by this ill-contrived law of settlements.¹⁶

But for all his love of free enterprise, Smith had some hard words for masters and merchants. Long before the American Civil War, he noted that slavery was a dying institution in view of its declining

economic feasibility, although it still flourished on sugar and tobacco plantations. Absence of incentives and the requirement of additional overseers were the main factors making slavery an increasingly dubious institution, even though Smith readily conceded that the master had to indirectly pay for the wear and tear of a free servant as much as or more than he had to pay directly for a slave. He wrote:

It appears, accordingly, from the experience of all ages and nations, I believe, that the work done by freemen comes cheaper in the end than that performed by slaves. It is found to do so even at Boston, New York, and Philadelphia, where the wages of common labour are so very high.¹⁷

On merchants, Smith wrote, in a line much quoted by those today prone to see monopoly and oligopoly as endemic to business enterprise:

People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.¹⁸

But the adherents of the "monopolistic competition" school who quote the foregoing rarely go on to quote Smith a few paragraphs later when he also noted:

In a free trade an effectual combination cannot be sustained but by the unanimous consent of every single trader, and it cannot last longer than every single trader continues of the same mind.¹⁹

For government, then, there was but a relatively small economic role in Smith's scheme of things. Government would be left with but three duties. For one, it would administer justice, and for another, defend against foreign or domestic foes. And, thirdly, it would erect and maintain certain public works and institutions which did not ordinarily lend themselves to operation

by private profit. Thus government could properly concern itself with such matters as lighthouses, street lighting, highway care, water supply, and public education.²⁰

Given these limited concerns, the cost of government would be *de minimus*, and excessive taxes imposed to cover wasteful superfluous public spending, including unnecessary wars, would go by the boards. To this end, he advocated four maxims on taxation:

1. The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state. . . .
2. The tax which each individual is bound to pay ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person. . . .
3. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it. . . .
4. Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the public treasury of the state . . . [so that it does not] require a great number of [revenue] officers, whose salaries may eat up the greater part of the produce of the tax . . . [or] obstruct the industry of the people, and discourage them from applying to certain branches of business which might give maintenance and employment to great multitudes.²¹

Smith also sensed how government tends to become more anti-consumer and aggressive under mercantilism, especially under the mercantilistic policy of colonialization and colonial trade monopolies. He wrote:

The monopoly of the colony trade, therefore, like all the other mean and malignant expedients of the mercantile system, depresses the industry of all other countries, but chiefly that of the colonies, without in the least increasing, but on the contrary diminishing, that of the country in whose favour it is established. . . . Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer. The maxim is so perfectly self-evident, that it would be absurd to attempt to prove it. But in the mercantile system, the interest of the consumer is almost constantly sacrificed to that of the producer; and it seems to consider production, and not consumption, as the ultimate end and object of all industry and commerce.²²

Certainly mercantilist roots, in one degree or another, can be spotted in the wars between England and Holland in 1652-54, and again in 1664 and 1672-74, the War of the Spanish Succession in 1702-1713, the war between Britain and Spain in 1739, the War of the Austrian Succession in 1740-48, and the French and Indian War beginning in 1754. Wars for what purpose? To what end? Wrote Smith:

A great empire has been established for the sole purpose of raising up a nation of customers who should be obliged to buy from the shops of our different producers, all the goods with which these could supply them. For the sake of that little enhancement of price which this monopoly might afford our producers, the home-consumers have been burdened with the whole expence of maintaining and defending that empire. For this purpose, and for this purpose only, in the two last wars, more than two hundred millions have been spent, and a new debt of more than a hundred

and seventy millions has been contracted over and above all that had been expended for the same purpose in former wars.²³

But for us Americans the supreme act of war against the mother country was yet to come. Come it did, with even the lower classes joining the merchant classes in seeking deliverance from British taxation without representation, from the inequities of primogeniture and entails, from paying for British trade monopolies and contorted trade routes, from the Coercive and Restraining Acts of 1774 and 1775 striking at the very heart of the economic life of the colonies, from, as the *Declaration* itself put it, George III erecting "a multitude of New Offices," sending "hither swarms of Officers to harass our People, and eat out their substance," and "cutting off our trade with all parts of the world."

Mercantilism, in sum, turned upside down the logic of trade from consumer sovereignty to producer sovereignty, from consumer benefit to producer benefit, from comparative advantage to comparative disadvantage. Politically, mercantilism led to unlimited government and continual warfare even though the government—George III or whoever—was supposedly the "visible hand" aiding and abetting the citizen and consumer. In effect, in bringing about the capitalist revolution, Adam Smith was pleading: Let my people—citizens and consumers everywhere—go; let them be comforted by private property, limited government, the "invisible hand" of peaceful trade and, in the idiom of our day, free enterprise. As Smith set forth:

As every individual . . . endeavors as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value; every individual necessarily labours to

render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he 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. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good.²⁴

But perhaps the prescience and power of

Adam Smith's mind is better seen in his discussion on America. Although he had completed his 900-page magnum opus well before 1776, he sensed some momentous development stemming from the mercantilist repression and republican spirit of the colonists, as can be seen in the following prophetic statement on the prospect of America (about to undergo both the American Revolution and the capitalist revolution):

From shopkeepers, tradesmen, and attornies, they (the American colonists) are become statesmen and legislators, and are employed in contriving a new form of government for an extensive empire, which they flatter themselves, will become, and which, indeed, seems very likely to become, one of the greatest and most formidable that ever was in the world.²⁵

¹Quoted by Ludwig von Mises in the introduction to *The Wealth of Nations* by Adam Smith, Gateway Edition, 1953, p. viii.

²*Cobbett's Parliamentary History of England*, XXIX, 1792, p. 834.

³Appleton, 2nd ed., 1866, p. 55. Contrast these glowing remarks to those of Max Lerner in introducing the Modern Library edition of *The Wealth of Nations*, 1937, p. ix: "Smith was . . . an unconscious mercenary in the service of the rising capitalist class in Europe. . . . he gave a new dignity to greed and a new sanctification to the predatory impulses."

⁴*De la Liberté du Travail*, quoted by Mill, *Political Economy*, V, xi, p. 7.

⁵Said Smith: "An injudicious tax offers a great temptation to smuggling." *The Wealth of Nations* (see *op. cit.*), p. 779.

⁶*The Writings of Benjamin Franklin*, edited by A.H. Smyth, IV, 1906, pp. 244-245.

⁷Smith, *The Wealth of Nations* (see *op. cit.*), pp. 651, 14.

⁸*Ibid.*, pp. 5-6.

⁹*Ibid.*, p. 13.

¹⁰*Ibid.*, p. 590.

¹¹*Ibid.*, p. 406.

¹²*Ibid.*, p. 424.

¹³*Ibid.*, p. 431.

¹⁴*Ibid.*, p. 438.

¹⁵*Ibid.*, pp. 121-122.

¹⁶*Ibid.*, p. 141.

¹⁷*Ibid.*, p. 81.

¹⁸*Ibid.*, p. 128.

¹⁹*Ibid.*, p. 129.

²⁰Smith obviously thought little of tenured education, complaining: "The endowments of schools and colleges have necessarily diminished more or less the necessity of application in the teachers. Their subsistence, so far as it arises from their salaries, is evidently derived from a fund altogether independent of their success and reputation in their particular professions. . . . [Indeed] in the university of Oxford, the greater part of the public professors have, for these many years, given up altogether even the pretence of teaching." *Ibid.*, pp. 717-718.

²¹*Ibid.*, pp. 777-778.

²²*Ibid.*, pp. 576-577, 625.

²³*Ibid.*, p. 626.

²⁴*Ibid.*, p. 423.

²⁵*Ibid.*, pp. 587-588.