

The Theory of Value. The great advance in economic thought which is due to Smith is the emancipation from mercantilist and physiocratic fetters. (For two hundred years economists had been searching for the ultimate source of wealth. The mercantilists had found it in foreign trade. The physiocrats had gone further and had shifted the origin of wealth from the sphere of exchange to that of production. But they had still remained confined within one particular form of production, agriculture.) Adam Smith, building on the foundations of Petty and Cantillon, effected the final revolution. With him labour as such becomes the source of the fund which originally supplies every nation 'with all the necessaries and conveniences of life which it annually consumes'. Smith still spoke of wealth in the sense of useful material objects, as his English predecessors had done, but, by making it result from labour in general, he was led to inquire into the social rather than the technical appearance of wealth. (The wealth of a nation, he said, will depend upon two conditions: first, the degree of productivity of the labour to which it is due; and secondly, the amount of useful labour, that is to say, labour productive of wealth, which is employed.) (The examination of the first of these factors leads Smith to the discussion of the division of labour, exchange, money, and distribution, to which the whole of the first book is devoted. The second involves an analysis of capital; and this is made in the second book.)

(Smith begins his analysis with the division of labour because he wishes to find the principle which transforms particular concrete forms of labour, which produce particular goods (use-values), into labour as a social element, which becomes the source of wealth in the abstract (exchange-value). (Division of labour becomes for Smith the principal cause of the increasing productivity of labour.) After giving his well-known account of its quality and consequences,<sup>2</sup> he proceeds to inquire into the causes which produce it. (It is here that he makes division of labour depend upon the propensity to exchange, which he regards as one of the principal motives of human conduct.) (There can be little doubt that on this point Smith confused

<sup>1</sup> *Wealth of Nations*, vol. i, p. 1.

<sup>2</sup> *ibid.*, Book I, ch. i.

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cause and effect. However true it may be that exchange cannot exist without division of labour, it is not true, at least in theory, that division of labour requires the existence of private exchange. It is logically demonstrable that a certain social organization (for example, the economy of a patriarchal tribe which lacks the institution of private property) can have a technology using division of labour without exchange. And communities of this type can be shown to have existed. Adam Smith was guilty of making the characteristics of the society of his own day valid for all time; he regarded as a natural human motive and made into a universal principle of explanation, a feature of the contemporaneous social order which was historically conditioned.<sup>1</sup> (But Smith's purpose was propagandist. (He emphasized the influence of the market on productivity in order to demonstrate that trade had to be freed as a prerequisite to the development of productive power, and not merely to the full use of the existing powers of production.)

(He proceeds to analyse how the degree of the division of labour is determined and concludes that it is limited by the extent of the market.) He elaborates points made originally by Xenophon, and later by Petty, and gives what has since been regarded as the classic description of the relation between the circle of exchange and the division of labour.<sup>2</sup> He shows that when these have reached a certain stage of development the dependence of each individual upon the rest of the community is very great. (Every man becomes then 'in some measure a merchant, and the society itself grows to be what is properly a commercial society'.<sup>3</sup> The efficiency with which this society carries out its now habitual exchanges must remain seriously defective so long as exchange is in kind. The well-known disadvantages of barter lead to the adoption of a generally accepted medium of exchange, money. Smith describes how the precious metals came to be chosen as the commodity of which money should be made, and briefly traces their progress through history. But this is only incidental. The important point to which the short discussion of money leads is the question of 'the rules which men naturally observe in exchanging [goods] either for money or

<sup>1</sup> *Wealth of Nations*, Book I, ch. ii.

<sup>2</sup> *ibid.*, ch. iii.

<sup>3</sup> *ibid.*, vol. i, p. 23.



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for one another. . . . These rules determine what may be called the relative or exchangeable value of goods.<sup>1</sup> In this rather roundabout way Smith reaches the central problem of his economic inquiry. But the problem was inherent in the very fact that he had started by abandoning the mercantilist and physiocratic concern with particular forms of wealth and proceeded to examine wealth in general as a social phenomenon.)

(Before beginning the analysis of value Smith distinguishes two uses of the word. One, he points out, signifies the utility of some particular object, and this he calls value in use; the other refers to the power possessed by an object of purchasing other goods: this he calls value in exchange.) He mentions a paradox in terms which have since become famous. Some of the most useful commodities, such as water, he says, have scarcely any value in exchange, while others, such as diamonds, although of little use, can command a great deal of other commodities in exchange (It was this paradox which was to provide the starting-point for the theorizing of economists of the later nineteenth century which finally led to the marginal utility doctrine.) Smith himself was not interested in elucidating the intricacies of use-value. He puts the distinction of the two meanings of the term 'value' at the end of his chapter on money in order, so it seems, to get it out of the way before beginning the really important work, the analysis of exchange-value. (This resolves itself into three parts: what is the measure of the exchange-value of commodities or, as Smith also calls it, their real or natural price? what are the constituent parts of this natural price? and, finally, how do variations of the market price of commodities from their natural price arise?) To these questions, chapters v, vi, and vii of Book I are devoted.

It is not easy to give a summary account of Adam Smith's ambiguous and confused theory of value. Subsequent economists have found two or three different strands of thought which Smith did not separate sufficiently clearly. He developed the labour theory inherited from Petty and Cantillon; but he also added to it certain elements of the supply and demand analysis of Locke. And in his struggles with the difficulties of the concept of capital and its place in the economic process he abandoned his own labour theory of value and bequeathed to later genera-

<sup>1</sup> *Wealth of Nations*, vol. i, p. 28.



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tions what became mainly a cost of production theory. According to their predilections economists have stressed one or the other of these different principles. But not even adherents of the same school can agree on their interpretation of Smith's theory. One writer, for example, is anxious to show the progress of the theory of value towards the subjectivist school to which he belongs; and he criticizes Adam Smith for having concentrated on the exchange-value (or purchasing power) of goods to the exclusion of their utility, which, to this writer, is the real cause of value.<sup>1</sup> A recent writer, on the other hand, who is also a follower of the subjectivist school, finds in Adam Smith traces of the beginning of that school. She thinks that Adam Smith, by adopting the consumer's concept of wealth, raised the problem of the connection between production and demand. (It was due, she says, to Smith's indecision in the treatment of this problem and to the subsequent victory of the Ricardian school that the demand aspect was neglected in England, and that that part of Smith's tradition was left to flourish on the Continent.<sup>2</sup>)

It is true that Adam Smith's theory is inconsistent. But although he involved himself, as we shall see, in many contradictions, he made considerable progress in the explanation of value. And, in the end, his theory rests on what Ricardo singled out as the basis for his own analysis; the labour theory of value. However inconsistent Smith may be in his exposition of it, he keeps to it most strictly in one important application of it—in his discussion of the surplus which formed the basis of all profit.

(It seems established that the earliest theory which Adam Smith held regarded labour as the sole source of value and the quantity of labour embodied in each commodity as the measure of that value.) But here, already, confusion begins. His discussion of exchange-value in the *Lectures* is little different from that of previous writers who had adopted a similar explanation. (Like Petty, Steuart, and Cantillon, he considered the value of a commodity to be determined by the cost of producing the amount of labour necessary for the production of the com-



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modity. This cost included not only the subsistence of the labourer himself but also allowances for education and reproduction. Like his predecessors, he admitted the influence of demand which determined the distribution of labour in such a way as to make value and cost of labour equal.<sup>1</sup>

(In the *Wealth of Nations* the theory is elaborated) but becomes less clear-cut. (In the first place, the scope of the labour theory becomes limited and an additional theory is developed in order to explain a further range of value phenomena. In the second place, the exposition of the labour theory itself, even within the limits in which Smith still admits its validity, is very confused.) The explanation of exchange-value in chapter v begins with an analysis of the quality of exchange-value derived from the social facts of division of labour and private exchange. (A man is rich or poor, he says, according to the amount of useful things which he can obtain. When division of labour has taken place his own labour can provide him with only a few of these things, and his wealth will come to depend on the amount of other people's labour which he can command.) The value in exchange of any commodity which he possesses will then be equal to the amount of labour it can command. (Smith concludes that labour 'is the real measure of the exchangeable value of all commodities'.<sup>2</sup>)

There follows immediately another account of the origin of value and its measure, which Adam Smith evidently intended to be only a version of the first but which is quite different. For he goes on to measure the value of a commodity not only by the amount of labour which it can command in exchange (or as he now puts it, the *value* of a certain quantity of labour), but also by the amount of labour which its production requires. These two explanations now persist side by side, ~~and the former~~