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- Welcome once again as MIT Professor Paul Samuelson discusses the current economic scene. This series is produced by Instructional Dynamics Incorporated.

- March 9, 1976 represents an important 200-year anniversary. The anniversary of the first publication of Adam Smith's Wealth of Nations. This 200-year birthday party is as important to the discipline of economics as the bicentennial 200th-year anniversary of the founding of the USA is to the citizenry of the United States. It is rare indeed that a scholarly discipline can trace its beginning to a single recognizable time and to a single recognizable author and to a single recognizable credence. But, I believe it is no exaggeration that the vast majority of economists would agree that Adam Smith represents so important a landmark, so important a break with the previous primitive developments in economics. So important a difference in degree as to constitute a difference in kind that Adam Smith can be regarded as the founder of economics in the same sense that George Washington can be regarded as the founder of our country or that VI Lenin can be regarded as the founder of the modern Soviet State. Adam Smith, I believe, is a living force, and I think that he is a rewarding writer to talk about quite aside from any feelings of piety because the matters which concerned him still concern economists today, and the precepts concerning the wealth of nations which he wrote about have continuing application into our times. So, let me paint something of the background of the 1776 Wealth of Nations, and let me relate that work to certain present day very lively debates. Adam Smith, of course, was a Scot. At the time of his youth from the 1720s on into the 1780s when he died, Scotland seemed to be a reservoir of brains for the British Isles. Doctor Samuel Johnson liked to jest about the Scots as if they were an eccentric, impoverished, rather over-intellectual group of people. But, I think the badinage of Doctor Samuel Johnson with respect to his disciple James Boswell and with respect to David Hume the Scottish philosopher and historian and Adam Smith is indicative of the envy and respect which Englishmen of that time held towards these Scottish thinkers. Smith was a bachelor all his life. I suppose the most romantic and exciting event in his life happened to him at the age of five or six when he was kidnapped by gypsies. However, he was restored to the bosom of his family in short order, and he went on to become a student in Scotland and a professor in Scotland and, unlike so many modern-day professors of economics, he was also a learned man of the world. He wrote a history of astronomy. He traveled on the continent. He was the tutor to the son of a nobleman. He had a sinecure in the civil service as a tax collector. But, what we remember him for today is not for his role as Mr. Chips, the lovable, genial, Scottish lecturer nor for the convivial Adam Smith who met with David Hume and other intellectuals to discuss philosophy and history and economics. We remember him for the founding of the subject matter of economics. Smith does not lack for admirers, but in some ways, his follower and successor of some fifty years later, David Ricardo, has tended to overshadow Smith in the textbooks of the history of economic thought. Smith is regarded as very early and very primitive, and, if I may say so, not very fancy. Any non-economist, any business man, any self-educated laborer could pick up Adam Smith's Wealth of Nations and read it with advantage. There are in it no bristling equations or graphs or tables. There are thousands, literally, of facts and observations. Smith was much better acquainted with all there was to know about industry in his time than your typical run-of-the-mill associate or full professor today, but at that time, economics was not a technical subject. By contrast, if you pick up the Principles of Economics of David Ricardo, you find a style of writing which is not very intelligible. You find numerical tables. It's anything but inviting fare for a non-economist. It's much more like an advanced economics treatise of today which no non-economist in his right mind would every think of picking up. Adam Smith is not only the father of economics as seen by economists but, what is quite another thing, he is also a very important figure in the history of ideas. Those are by no means the same thing. Alfred Marshall of the University of Cambridge from, let us say, 1885 until he died in 1920 would probably have been revered as the greatest economist of his time. And yet, if you spend a lifetime, as I have done, in reading intellectual history, you will not be able to find more than one or two or three references to the work of Alfred Marshall outside of the technical field of economics. Alfred Marshall thought that his 1890 Principles of Economics, which was an important best seller in the field for many years, was written for businessmen, but the evidence is remarkably lacking that businessmen ever outside of command performances in school bothered to read Alfred Marshall's Principles of Economics. Not so with Adam Smith, any educated person of his time and since could hope to dip into Adam Smith not only with pleasure but with advantage. What is the stereotype role in the history of ideas that Adam Smith is thought to have played? Well for once, the vulgar stereotype comes very near the true mark. Adam Smith came at a time when government over-regulation of industry was on its way out, and Smith was both an effect of that process and, in his own right, an important cause. He analyzes in great detail the follies of government interference. He extols the merits of freedom, of laissez-faire, so by large the notion of Adam Smith as the apologist for laissez-faire, for the rising bourgeoisie class, Smith as the critic of the dying futile order, as no lover of the land owner, I think that that particular stereotype is a pretty faithful rendition of what it is that is important about Adam Smith. Now, nothing that I have said contradicts the notion that Adam Smith was a humane, eclectic and temperate man in his ideologies. You can easily in an afternoon with The Wealth of Nations, by they way, there's a very convenient edition of The Wealth of Nations in the Modern Library Series adapted by Edwin Cannan, an English economist of the last generation or two, you can cull passages from Adam Smith which show him to be no reactionary, no friend of the plutocratic interests. I have in mind passages like this, masters never meet even for the purposes of innocent merriment and dinners but what they plot against the public interest. These could've been marvelous anticipations of Judge Elbert Gary's famous dinners in which he brought together executives and tycoons in the steel industry, and in the course of what was probably a very good meal, they conspired on maintaining prices above a competitive level. Smith was also very much acquainted with the monopolies which the budding trade union movement was trying to create. Smith did have certain limited functions for government. If somebody had said to Smith, should the government have an anti-trust division to police departures from perfect competition, Adam Smith would probably have replied, in principle, monopoly is bad. In principle, successful regulation which reduced the degree of monopoly and achieved a greater approximation to free competition would be good, but in practice, now in 1776 or 1783 at the time of the second edition, my considered opinion is that the government'll pry make things worse if it tries to interfere in this matter. Well, there's many an economist today, prominent, respected economist, who has moved to this new position or back to Adam Smith's old position. I think it's fruitless to try to decide where Adam Smith would fit in in today's ideological spectrum if he were brought back to life. Given where he stood at the time of the 18th century, it might well be the case that he would be at exactly that golden central position that I myself try to occupy. But, it would be self-deception and self-flattery to assert that to be the case, and I'm sure that people both to the left of me and to the right of me, when they engage in their contrafactual reconstructions of intellectual history and bring Adam Smith back to life, they find that Adam Smith turns out, with all his wisdom, to be almost precisely where they, with all their wisdom, have decided it's best to be. Now, I'm the more reminded of this centennial because we are right now, in the economics profession, along with the nation's bicentennial having a whole series of commemorative symposia and meetings to honor the memory of Adam Smith. In Scotland in March, there will be a gathering of Adam Smith experts from all over the world. Professor George Stigler of the University of Chicago will be there. Professor Charles Kindleberger of MIT will be there. And, at Harvard University February 27th and 28th, there were held the John Diebold lectures called New Challenges to the Role of Profit. This was a Harvard series, the fourth series of John Diebold lectures since the late 1960s, addressed this time to the role of profit, and it turned out that quoting Adam Smith and analyzing and criticizing the positions of Adam Smith with respect to the rate of profit was very widespread, and I must say very appropriate. I myself was the first of three major lecturers. I spoke about the role of profits in a mixed economy, changes in the perceived reality. Well, that was my assigned title, but the title that I chose actually to address myself to was the views of profit as seen by the modern-day economist and by non-economists, and a good deal of my discussion could profitably begin from a discussion of Adam Smith's division of the national income of society into three or four major components, on the one hand the wages of labor, on the other hand the interests, interest rate, interest earnings on capital, on produced inputs, the rent of land. Then, as distinct from the sure thing, safe competitive rate of interest, there is a fourth component which might be called differential profit. Adam Smith, Smith himself said that the rate of interest is about five or 6%, and the rate of profit typically is about double that, about 12%. Why this difference? Part of it, obviously, was the wages of scarce, valuable, managerial talent. Part of it was a allowance for risk. When you make a lot of money on one shipping venture, you must realize that the pickings aren't all that easy and certain, and that on some other shipping venture, people are losing money, so the average premium for risk-taking over and above the safe gilt-edge rate of interest would be much less, one would suppose, than a doubling of the gilt-edge rate of interest. In Adam Smith's day, we didn't have to talk about pre-tax and post-tax rates of profit because by and large, although Smith himself was a tax collector part of his life, the taxes to British Isles depended upon, and other countries depended upon, were largely excises and not income taxes. In our own day, Frank Knight, famous professor at the University of Chicago just recently dead in his late 80s, argued that people are not risk adverse, and that the premium for risk-taking need not be a positive premium. It might be zero or might even be negative as people will pay for the privilege of gaming and of taking risks. I think the bulk of the data on the stock market, when we come to analyze it, suggests that, on the whole, people are risk takers even though they do spend some weekends in Las Vegas. Smith's general notion was that any excess profits that couldn't be accounted for by some real cost would in the longer run be competed away. And, his view of the national income, and indeed of the components of the price of any good, was essentially a three-fold view. The price of any good involves a return to labor which is a needed compensation for the psychic sweat or disutility of working. The interest and profit component, we can consider those to be the same if there is no riskiness in the situation, no probabilistic uncertainty. Smith would have agreed with Nassau Senior who came along some half a century later that there was a certain amount of unpleasantness involved in giving up today's current consumption in return for future consumption. If one gives up 100 chocolates or 100 baskets of goods today, as compensation, for the psychic disutility of doing so, one must not only get back one's principle of 100 chocolates next year or 100 baskets of goods next year, but one must get some premium for the psychic disutility of waiting or abstinence. The third big component of price and of national income, the return to land rent, which Smith, like some of the earlier physiocrats in casual moments seem to think there were three major classes who got three different kinds of income, he thought of these as 1/3, 1/3, 1/3, just the way you might say on a typical farm. 1/3 goes to the landowner, 1/3 to the operator and 1/3 to the labor, that was his view of the GNP. Well, this third component Smith regarded as an undeserved component. The land itself is productive, yes. It is indispensable for production, yes. But, the landowner is not indispensable. He's quite dispensable. As Smith said, landlords like to reap where other men have sown. So, Smith would've been very much in the tradition both of the physiocrats before him and of Henry George and Ricardians after him of wishing to tax, if you can identify it, the return to pure land, the pure Ricardian rent, the return to the original, inexhaustible, unaugmentable gift of nature. Now, the return to land which had been improved by draining and by investing of capital into it, Smith would've regarded as interest much like other interest, but this original return to raw land, the pure rent component, he thought of as not a necessary component of price. Well, Smith was not only a statical economic theorist, he also had a vision of progress and of what was happening over time. In his view, the future of the capitalistic order in the century let's say after 1776, 1783, would be a century of capital accumulation. He believed that the rate of profit, the rate of interest was lower in Holland than in the British Isles because over past decades, the Dutch had thriftily accumulated capital, had used up all the high-profit opportunities and now were reduced to building bridges and dikes which would yield only a low profit, and he thought the same thing would happen to Britain. Smith was a believer in the doctrine that it is better to travel than to arrive. He thought the process of growth would be a happy state in which wages would not be ground down to the minimum. As long as an economy was progressing, he believed the workers would be sharing in a rising standard of living higher than the bare minimum of subsistence. But, once accumulation ceased, the remorseless biological increase of population would, in a fashion that Malthus later was to make popular and which Ricardo was to analyze and detail, would cause there to be a reduction in wages. Now, I've commented that Smith was a very well-informed person for his time, but we must remind ourselves how little the best informed man in the world knew about what was actually happening. Smith thought, for example, that India had had a higher standard of living in the past than was true at that time when he was writing and higher than that in Western Europe. Probably, both of those statements are questionable, and one of them definitely untrue. My colleague Professor Kindleberger is arguing in Glasgow in March that although Smith lived just as the industrial revolution was popping out all over in its most acute takeoff form, he was remarkably unaware of that industrial revolution, and then most of the homely examples he gives are taken from library books rather than from real life and from earlier library books, that is books of earlier date. Smith thought that the tendency would be for a falling rate of profit. A view which was shared later by David Ricardo, and curiously enough, by Karl Marx. And which, at the John Diebold lectures, many of the economists and discussants present, I should say there were no less than nine discussants there, they seemed on the whole to agree that within the last decade or two, there has indeed been, in the modern economic societies of the affluent West, a downward trend in the rate of profit even though the history of our times of the period since 1776 has, on the whole, been a meandering of the rate of real interest without much trend, definite trend upward or downward. How could one account for this? Well, Smith would not have been greatly surprised because Smith unlike David Ricardo put a great deal of emphasis on technological change, on the division of labor, and so what you've had is a Schumpeterian process, a dialectical process in which innovation has tended to raise the rate of profit and accumulation has tended to lower it with more or less a Brownian vibration or wobble of the rate of profits from time in the last 200 years. How remarkable it is that one can profitably spend half an hour in discussing the thinking of somebody who died almost 200 years ago. That, I think, is the real test for seminal influence by a writer, and Adam Smith passes that test with flying colors.

- If you have any comments or questions for Professor Samuelson, address them to Instructional Dynamics Incorporated, 450 East Ohio Street Chicago, Illinois 60611.