Markets Natural and Artificial in Adam Smith

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Jessie Norman's *Adam Smith: Father of Economics* is filled with fascinating facts about Smith and his life, and it does a fine job placing Smith and his work in the proper historical, philosophical, and economic context. As Norman rightly emphasizes, "for Smith markets and moral behaviour are generally mutually enabling" (p. 235), but that does not mean that Smith believes "commercial society is in any way perfect or in some state of grace" (p. 236)—crucial points that many who wish to bend Smith to their own aims often miss.

In this brief note, I would like to address another important point Norman makes in connection with Smith's conception of markets, namely that "they are not purely natural, in the sense of arising simply from God or nature" (p. 242). Norman continues: "there is no theoretical state of nature for markets, and there never was a historical one. Markets have no natural or scientifically determinable boundaries: they are human constructs" (p. 243). Partly on this basis Norman goes on to argue that Smith was not only not a proponent of "crony capitalism" (p. 271), but also that Smith was neither a proponent of a crabbed "homo economicus" conception of human nature (p. 291) nor was "a market fundamentalist, an economic libertarian, or in that strong sense a *laissez-faire* economist" (p. 324). Indeed, according to Norman, Smith did and would endorse "careful regulatory interventions" into the market (p. 286) intended to "lift human capabilities and improve the capacity for human interaction, communication, and mutual recognition" (p. 319).

Norman is correct that Smithian markets are "human constructs"—they do not exist, after all, without human action. Yet there is also an important sense in which Smith believes markets, as well as the decisions people make within them, are natural. In several places Smith expresses wariness about the kinds of regulatory interventions into markets that Norman recommends, not only because of the limits Smith believed human knowledge faces (something Norman recognizes) but also because Smith seems to think that such "artificial" interpositions violate what he calls our "natural liberty" and frequently lead to worse, not better, results than allowing for the "natural" course of things.

Smith repeatedly adverts to a notion of 'naturalness' in *The Wealth of Nations*.[1] (Indianapolis, In.: Liberty Fund, 1981; hereafter, "WN"). As Norman cites, Smith advocates an "obvious and simple system of natural liberty"; this "natural" system arises when every person "is left perfectly free to pursue his own interest his own way, and to bring both his industry and capital into competition with those of any other man, or order of men" (WN, 687). Smith contrasts this "natural" system with "every system which endeavours, either, by extraordinary encouragements, to draw towards a particular species of industry a greater share of the capital of the society than what would naturally go to it; or, by extraordinary restraints, to force from a particular species of industry some share of the capital which would otherwise be employed in it" (WN, 687). What Smith calls "extraordinary encouragements" and "extraordinary restraints" are for Smith artificial and thus in conflict with what is "natural." The problem with artificial interposition, according to Smith, is that it is "in reality subversive of the great purpose which it means to promote. It retards, instead of accelerating, the progress of society towards real wealth and greatness; and diminishes, instead of increasing the real value of the annual produce of its land and labour" (WN, 687).

Those are strong words, but they are not isolated. Elsewhere in WN Smith writes: "No regulation of commerce can increase the quantity or industry in any society beyond what its capital can maintain. It can only divert a part of it into a direction into which it might not otherwise have gone; and it is by no means certain that this artificial direction is likely to be more advantageous to the society than that into which it would have gone of its own accord" (WN, 453). In fact, Smith gives us positive reason to believe that "artificial" regulation would lead to deleterious consequences. According to Smith, "every individual, it is evident, can, in his local situation, judge much better than any stateman or lawgiver can do for him" how he should allocate his resources (WN, 456). Individuals have knowledge of their own resources, of the opportunities available to them, and of their own schedules of value and purpose that a legislator, statesman, or regulator will not possess. That puts individuals in a relatively better epistemic position than are legislators to know what decisions individuals should make, given the constraints they face, about how to achieve their ends. Moreover, Smith argues, every "individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of the society, which he has in view. But the study of his own advantage naturally, or rather necessarily, leads him to prefer that employment which is most advantageous to the society" (WN, 454). For that reason, Smith writes, a statesman "who should attempt to direct private people in what manner they ought to employ their capitals, would not only load himself with a most unnecessary attention, but assume an authority which could be safely be trusted, not only to no single person, but to no council or senate whatever, and would nowhere be so dangerous as in the hands of a man who had folly and presumption enough to fancy himself fit to exercise it" (WN, 456). Strong words indeed—and, it would seem, a strong caution against the kind of artificial "careful regulatory interventions" Norman suggests Smith would endorse.

Smith uses the language of "natural" vs. "artificial" throughout his writings, including not just in WN but also in his *Theory of Moral Sentiments* and his *Lectures on Jurisprudence*. But to focus only on WN, Smith advocates, for example, "a society where things were left to follow their natural course, where there was perfect liberty, and where every man was perfectly free both to chuse what occupation he thought proper, and to change it as often as he thought proper" (WN, 116). Smith frequently connects his idea of the "natural course" of things with the liberty of individuals. For example, "But the policy of Europe, by not leaving things at perfect liberty, occasions other inequalities of much greater importance," including "by restraining the competition in some employments to a smaller number than would otherwise be disposed to enter them," "by increasing it in others beyond what it naturally would be," and "by obstructing the free circulation of labour and stock, both from employment to employment and from place to place" (WN, 135). Again: "Let the same natural liberty of exercising what species of industry they please be restored to all his majesty's subjects, in the same manner as to soldiers and seamen; that is, break down the exclusive privileges of corporations, and repeal the statute of apprenticeship, both which are real encroachments upon natural liberty, and add to these the repeal of the law of settlements, so that a poor workman, when thrown out of employment either in one trade or in one place, may seek for it in another trade or in another place" (WN, 470).

Such examples could be multiplied, but perhaps they suffice to reflect Smith's repeated aversion to "artificial" intervention into the market. Smith's argument seems to be that when third parties intervene in others' decisions about allocating their resources, choosing their vocations, accepting or declining employment, and so on, not only does it violate the "natural liberty" of first and second parties to make such decisions on their own but it also leads to inferior results. The latter ensues because third parties do not possess the "local" knowledge that first and second parties do but that is required to make good decisions. For third parties to believe otherwise is, according to Smith, "folly and presumption."

Now, Smith might be wrong about all of this, or at least some parts of it. For example, there might be cases in which legislative or regulatory intervention into markets is necessary to address the "intrinsic weaknesses" (p. 328) of commercial society that Norman articulates, including such things as "imperfect information, limited human rationality, preference-formation and transaction costs" (p. 331). And, as Norman rightly emphasizes, Smith himself acknowledged a duty of government of "erecting and maintaining certain publick works and publick institutions" (WN, 687–8), including infrastructure and limited public support for elementary education. Thus, as Norman again rightly argues, Smith was not wholly or naïvely anti-state or anti-government. Smith supported a robust state for the protection of "justice" against both foreign and domestic aggression, as well as to address the "certain publick works and publick institutions" he thought would benefit substantially all citizens but could not be provided by private enterprise. As Norman shows, Smithian markets require protections of the persons, the property and possessions, and the voluntary agreements and contracts into which people enter, and this, Smith thought, was the primary purpose, even the *raison d'être,* of the state. For all that, however, Smith nevertheless also seemed to believe that people would 'naturally' make better decisions about how to allocate their own time, talent, and treasure than legislators or regulators could 'artificially' do for them, and that the resulting 'natural' flows of capital would tend to benefit not only the individuals themselves but would also "promote the publick interest" (WN, 456).

NOTES

1 Adam Smith. *The Wealth of Nations*. (Indianapolis: Liberty Fund, 1981; hereafter, "WN").