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Business Ethics in Adam Smith’s works*

Abstract

This paper presents some views of Adam Smith based on some selected problems of business ethics. These can be found in his famous works—The Theory of Moral Sentiments and The Wealth of Nations—and in his lectures at the Glasgow University, where he was a professor of moral philosophy in 1752–1764. The main argument of the paper is that ethical problems (presented mainly in The Theory of Moral Sentiments) are also present in his political economy, which contradicts some neoliberal interpretations of his works as ones of the “intellectual father of capitalism”. In The Wealth of Nations, Smith criticizes each social class because of the fact that its interests are incompatible with the good of the whole society. He condemned the monopolist efforts of the traders and entrepreneurs, described some property owners as “vain egoists” and advanced the interests of the poor. He maintained that the interests of the traders should be supported when these were compatible with the interest of the consumers. The desire for possession and wealth should be analyzed from the social point of view: It is good when it contributes to the common good and the reproduction of humankind.

Keywords: Adam Smith, Das Adam Smith Problem, ethics of economic life, business ethics

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1. Introduction

Adam Smith (1723–1790) was a professor of moral philosophy at the University of Glasgow between 1752 and 1764. At the time, moral philosophy was not limited to just ethics, it also encompassed a series of disciplines that are nowadays considered separate areas of study.¹ In Smith’s view, moral philosophy consisted of four domains: natural theology (proofs for the existence and attributes of God), ethics, justice and jurisprudence. The last one also contained political theory, including investigations concerning the increase of wealth and prosperity of the state, which was then called Political Economy. The adjective political did not refer to contemporary political affairs but rather to the Greek, a term used by Aristotle to describe the knowledge or skill (art) of governing a state (cf. Narecki, 1994).²

In 1759 A. Smith published The Theory of Moral Sentiments, his first masterpiece, which was an extensive collection of his lectures on ethics, devoted mostly to moral philosophy. Smith intended the book to be a part of a larger project, eventually, however, the second and last part of the intended cycle was published in two volumes in 1776 and was titled An Inquiry into the Nature and Causes of the Wealth of Nations, better known under its shortened title, The Wealth of Nations. It is noteworthy that the first ideas it describes were mentioned in Smith’s lectures on jurisprudence. In the last years of his academic work, he focused his investigations in this domain.

Today, Adam Smith is famous as the author of The Wealth of Nations, the work that earned him the title of “father of economics” and recognition in the economic textbooks that followed. However, Smith is mainly famous for a few well-known sayings, often taken out of their context and not always properly quoted. Very few read the thick volumes of eighteenth-century philosophers.

In the last 35 years, the works of Adam Smith and his students’ notes have been thoroughly investigated.³ The University of Glasgow played an important role by celebrating the 200th anniversary of the first edition of The Wealth of Nations. This initiative created a 6-volume The Glasgow Edition of the Works and

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¹ Philosophy at British universities was traditionally divided into natural and moral philosophy. The former included natural sciences, the latter disciplines dealing with human beings (as individuals and collectives).
² The term “political economy” was introduced by A. Montchrétien de Vatteville in his Traité de l’oeconomie politique (1615). He wanted to emphasise that his treaty pertained to the state economy and not the household economy like Oikonomikos by Xenophon, and so he added the adjective “political”. In the Encyclopedia, in the article De l’économie politique (1755), J.J. Rousseau pointed to the ambiguity of Latin oeconomia (from Greek oikonomia), by making a distinction between “domestic economy”, i.e. “private”, and “general economy”, i.e. “public” or “political”. He dealt with the latter and understood it as governing (executive power) and he discussed the economic issue only in the context of state revenue. J. Steuart published Inquiry into the Principles of Political Economy (1767), which Smith knew but did not refer to, although in one of his letters he promised a critical analysis of all his “false claims”. Smith did not use the term “political economy” in his work probably because Steuart used it before him.
³ Before his death, Smith demanded all his manuscripts should be burnt.
Correspondence of Adam Smith (GEWCAS), published between 1976 and 1983 by Oxford University Press (Zabieglik, 2003, pp. 202–203). Since 1995, the International Adam Smith Society has published a scholarly, peer-reviewed journal, The Adam Smith Review. Every year, numerous publications are devoted to different aspects of Adam Smith’s work, including issuing of new editions and translations of his works. Smith’s work is being revived and studied in countries around the world (cf. e.g. Zabieglik, 2002, pp. 168–183).

2. The Theory of Moral Sentiments

The work, Theory of Moral Sentiments (1759) consists of seven parts. The first part deals with issues regarding the propriety of actions. The second section addresses the questions of merits and demerits, rewarding proper and punishing improper actions. The third part relates to justifying one’s judgments of sentiments and actions, and the sense of duty. In the fourth part, Smith describes the consequence the utility has on moral approbation (here, he argues with David Hume, among others). In the fifth part, he takes on the influence of habit and fashion on the feelings of approbation and disapprobation. In the sixth part, he goes on to describe the character of virtue. Smith added this particular section in his 1790 edition. The final section (Part 7) is a stand-alone piece, not directly connected to the other six sections. In all likelihood, the final chapter is an introduction to his lectures on ethics. The work reads as a light essay, is characterised by quite extensive narration and abounds in digressions and remarks about various spheres of social life.

Smith’s main claim is that people judge the actions of others first, and only then do they apply these judgements to their own actions. The source of these judgements is a certain kind of feelings—moral sentiments. People are moral beings because they experience sentiments that they can co-experience with others.

Smith claims that humans have a special ability—an ability to feel sympathy towards other humans. He labels this ability as fellow-feeling and extends it by adding other similar emotions, e.g., compassion.

Pity and compassion are words appropriated to signify our fellow-feeling with the sorrow of others. Sympathy, though its meaning was, perhaps, originally the same, may now, however, without much impropriety, be made use of to denote our fellow-feeling with any passion whatever. (Smith, 1759/1989, p. 8)

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4 Since the fourth edition, The Theory of Moral Sentiments had a subtitle: An essay towards an analysis of the principles, by which men naturally judge concerning the conduct and character, first of their neighbours, and afterwards of themselves.

5 Smith uses several terms that are translated into Polish as “uczucie”. Often, these are, sentiment and passion, but one also finds affection, emotion and feeling. Hochfeldowa (1975, s. XI) remarked on the “ambiguity of the English word sentiment, which means […] not only an emotional state but also a disposition, attitude, approach, opinion and even a belief.”
Misunderstandings about the philosophy of Adam Smith usually arise from a superficial understanding of this term. Sympathy is a trait of character identical to kindness. It is assumed that Smith attributes sympathy to every human being as a natural quality. However, for Smith, sympathy is primarily an ability of feelings to spread, a sensual echo, a psychological phenomenon that explains the shaping of moral judgements. When the spreading of feelings such as happiness or sorrow is accompanied by kindness, helpful behaviour, and positive attitude of the observer toward the experiencer, one may also use the term sympathy in the way it is used in Polish.  

“Although sympathy lies in the nature of men”—writes Smith—“they will never comprehend that which happened to the other” (Smith, 1759/1989, p. 26). If harmony of feelings, which is the foundation of social life, is to appear, the experiencer must adjust the extent of their emotional expression to the perceptual abilities of the observer. Under ideal circumstances, the levels of emotions become even. The phenomenon of sympathy is transitive in character: People adopt their perspectives to those of others.

In the situations analysed by Smith, one encounters the quality of propriety and the feelings associated with such attitudes and behaviour. Its measure is a psychological criterion (how comparable are the emotional re-echo of the observer and the experience of the experiencer) or a sociological one (common acceptance of a given thing as appropriate). Because they can often be insufficient due to, say, subjective factors, the lack of full understanding of their causes, etc., Smith introduces the concept of an impartial spectator. Although he does not devote a chapter to the idea, the concept plays a crucial role in his ethics. An impartial observer, contrary to the majority of ordinary observers judging human attitudes and behaviour, has full knowledge about the judged individual, especially about the causes of their actions and their intentions. They are also completely devoid of any emotion that could warp their judgement. However, they are not heartless, i.e. they have the sensitivity that enables them to immerse themselves in the feelings of the judged. An impartial spectator is another self that looks at us from a perspective and judges our actions without emotions and egoistic interest. Their voice cannot be stifled. Smith often refers to such a hypothetical observer and asks how they would judge a given deed. Despite the sophisticated conditions an impartial spectator must meet, Smith thinks that most of the humans can play such a role. As an example, he offers that a spectator’s judgements are often identical to moral judgements dominating in the society. Thus, the society is a mirror in which the individuals see the moral qualification of their actions. Using psychoanalytic terminology, we can say that the concept of an impartial spectator tried to explain how the instinctive desires of individuals are socialised by their superego.

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6 The ambiguity stemming from the many meanings of the term sympathy could be resolved if the term sympathy meaning an emotional re-echo was replaced by empathy, introduced at the beginning of the last century by psychologists (cf. e.g. Rembowski, 1989).

7 An example of the latter could be the amount of respect that rich people enjoy, contrary to those of lower status or with less money, although “the claim that wealth and greatness in themselves deserve respect does not correspond to moral principles and even the criteria of proper rhetoric” (Smith, 1759/1989, p. 89).
3. The Wealth of Nations

In the foreword to the sixth edition of The Theory of Moral Sentiments (1790), Smith referred to his earlier endeavours to write about “principles of law and government, and of the different revolutions which they had undergone in the different ages and periods of society; not only in what concerns justice, but in what concerns police, revenue, and arms, and whatever else is the object of law. In the Inquiry concerning the Nature and Causes of the Wealth of Nations, I have partly executed this promise”.

Among the notes of one of his students from 24 December 1762, one finds that Smith opened his lectures on jurisprudence by saying that having achieved nation-wide peace „the government will then strive to promote the wealth of the state. It leads to actions that we call police. All regulations regarding crafts, trade, agriculture and manufactures of the country are treated as belonging to police” (1978, Vol. 5, p. 5). Smith addressed the same issue again in the lectures of the following academic year:

The objects of police are the cheapness of commodities, public security and cleanliness, if the two last were not too minute for a lecture of this kind. Under this head, we will consider the opulence of a state.

It is hoped that the two quotations, provide an answer to a recurrently asked question: How come a moral philosopher pens a book that makes him the “Founding Father of Economics”?

In The Wealth of Nations, Smith developed some bold ideas about several important economic concepts and economic policy. He peppered his writing with illustrating, examples and digressions. The book was an instant success in the U.K. and abroad. His easy-to-read style provided the book the momentum and depth that other books on economy lacked. Economy—looking for scientifically understood strictness and specialisation—had cut its ties with philosophy. The comprehensiveness of Smith’s work with an in-depth analysis of the British and the global economy, and his insight into the nature and rules governing the economic processes in the chaotic actions of the manufacturers and consumers, all this, aided with numerical data—made The Wealth of Nations a text in economics rather than philosophy. His writings are essential readings not only for the economists but also for the students of economic theory.

In a brief introduction to The Wealth of Nations, titled Introduction and Plan of the Work, Smith outlines the key topics of the book:

Book I: The causes of improvement in the labour productivity, and based on the different ranks and conditions of people in the society, the system of distribution of the goods and services produce.

Book II: Capital stock, how it is accumulated, and of the different quantities of labour that are utilized for production.
Book III: A discussion of the conditions introduced and established during and since the fall of the Roman Empire. These practices have become the dominating forces in the economic policy of Europe favouring the arts, local trade and industry, and the commerce of towns while neglecting agriculture and the industry of the country.

Book IV: Theories of political economy; some magnify the importance of the industry carried out locally, others that are carried on in the country and the principal effects these have produced in different ages and nations.

Book V: Who should pay various expenses in a society? If something is beneficial to the whole society, the expenses ought to be defrayed by the general contribution of the whole society. If something benefits only a few, then, that particular group should be responsible for the expenses. Nearly all contemporary governments use such a rationale for the creation of wealth, allocation of its labour and resources for production and distribution. Translating it into modern economic jargon, the first two books are devoted to introducing an economic theory whose main area of focus is economic growth. Smith analyses various aspects of producing, exchanging and accumulating goods, especially: the division of labour, the use of money, the types and parts of price, wages of labour, capital gain, the rent of land, accumulating and allocating capital.

The economy analysed in theoretical parts of The Wealth of Nations was the developmental stage that Smith called: commercial with agriculture, manufactures and trade as its main elements. Since exploiting land was subject to land rent, Smith included mining in agriculture. However, he did not include services, the so-called liberal professions (lawyers, teachers, doctors, literary writers, etc.) and non-manufacturing areas connected with the activity of the state (the court, the clerks, the justice system, the army and the fleet, the clergy, etc.).

In a society where “things go in a natural way”, the foundation of its economy is a free market of manufacturers and consumers. The manufacturers compete for consumers; the consumers select the goods that maximize their utility—the core principle of free competition. The sellers try to get the best prices while the buyer try to pay lowest prices. Competition and free market are the mechanisms of a self-regulating economy. These become instrumental in the allocation of capital and labour. A measure of effectiveness of such allocation is the rise of a nation’s wealth, i.e. the annual produce of the land and labour of the society.

Smith’s model of economy assumes full employment and optimal utilisation of all resources of the society. In a state of “absolute freedom”, the annual produce of the land and labour of the society would increase every year unless the occurrence of some unusual spending such as wars, natural disasters, or the profligacy of the government. Naturally, in an agricultural land, its people would allocate their capital in agriculture rather than in industrial manufacturing, internal trade, international consumption trade, and in transit trade. However, in modern Europe, Smith argued, such a natural order was reversed.
When presenting his theoretical models, Smith often refers to the state of economy in Britain and other countries, pointing to various discrepancies between theoretical analysis and economic reality. For instance, describing the incongruities of import regulations in various countries, Smith (1776/1954, Vol. 2, p. 68) observed:

To expect, indeed, that the freedom of trade should ever be entirely restored in Great Britain is as absurd as to expect that an Oceana or Utopia.

When writing about the ban on British craftsmen to work in other countries, Smith describes such a regulation as “contrary [...] to the boasted liberty of the subject, of which we affect to be so very jealous; but which, in this case, is so plainly sacrificed to the futile interests of our merchants and manufacturers” (1776/1954, Vol. 2, p. 355).

4. Ethical aspects of economic life

When building his economic theory and postulating ideas on economic policy, Smith bases them on various claims and assumptions regarding the nature of man and social phenomena. He often confronts the consequences drawn from this theory with the socio-economic reality of Great Britain and of other countries, both in his contemporary times and in the past. Smith, conducting his economic analyses, often refers to the society in which “things are left to follow their natural course, where there is perfect liberty”, and people are characterised by care for their own interests. In such circumstances, individuals: a) have perfect liberty to make economic decisions and to choose or change their professions; b) make rational decisions, considering their own interests; c) trying to realise their private interests, i.e. seeking their own profit, they contribute to the realisation of the good of the general population, as if directed by an “invisible hand”.

The last sentence constitutes a premise of the concept of social harmony, within which it is possible to reconcile private interest with the interest of the whole society. If there is a conflict between them, Smith considers the interest of the whole society to be more important. In his theory, the concept of the good or the interest of the society is limited to the domain of economy and is usually equivalent to anything that increases the national income. The interest of all consumers is more important than the interest of particular manufacturers.

9 Nowadays, the metaphor of “the invisible hand” means a self-sufficient market mechanism. Smith understood it more broadly as a—deistically understood—most general rule ensuring social harmony.
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. (Smith, 1776/1954, Vol. 2, p. 355)

Social good also includes everything that pertains to the country’s defence capability. It can justify deviations from the principle of economic freedom such as prohibitions or regulations on the one hand and monopolies and preferences on the other. It is because national defence is more important than caring for the nation’s wealth.

The freedom to make economic decisions means for Smith that employed workers can change jobs at any moment, landlords can change the conditions of the lease, and the owners of capital can allocate their resources in any enterprise they deem appropriate. Perfect liberty has its limits, though. The state can ban a few individuals from exercising their natural freedom if their actions pose a threat to the safety of the whole society. Such limitations can also pertain to economic activity.

Smith treats the division of labour as a driver of efficiency, and a symptom of social nature and people’s propensity for trade and exchange. To satisfy these needs, especially in a civilised society, people need cooperation of other people—a cooperation based not on kindness but on mutual gains, i.e., the maxim: “Give me what I want and you will get what you want”. By appealing to people’s egoism, one can offer them one’s services or products provided that they, in return will offer something of value (money) to the producer. This exchange facilitates the division of labour, encouraging people to focus on their particular professions and sharpen their talents and skills. Without such a division, people would have to do many things for themselves rendering an economy less efficient.

Smith also noted some negative aspects of advanced division of labour where a labourer performed the same activity repeatedly. Binding a worker to one type of activity comes at a cost of their intellectual capacity, limits their social life, and decreases their military potential. To prevent “near complete demoralisation and degeneration of the population” performing such work, Smith postulates, in Book V of The Wealth of Nations, that the state should introduce universal education at primary level (reading, writing, basic mathematics).

Smith called the stage of an economic development of a given country where citizens satisfy their needs by means of money—a goods market or a commercial society. Such a society is characterised by a development of industry, local and international trade, and extensive division of labour. Such a society is capable of providing welfare of its citizens, a variety and abundance of goods and services, a developed legal system that regulates ownership, and the state revenues through tariffs and taxes. The end result is that the agreements and obligations are honoured through honest and fairness in decision-making while kinship bonds become of secondary importance. On the subject of jurisprudence, Smith mentioned several positive phenomena accompanying commercialisation of social life—e.g., development of sciences and skills and the rise of general well-being. Smith also
pointed to the negative dimensions such as: (1) “Trade spirit” limits people perspectives and advanced division of labour prevents the workers from developing many of their potential abilities, especially their intellectual potential; (2) Children’s education is neglected because the children are often sent to work; uneducated workers spend their leisure time fighting, drinking and debauchery, thus living in poverty; (3) Military spirit fades; the duty to defend the country falls to professional armies (often hired).

These are the disadvantages of a commercial spirit. The minds of men are contracted, and rendered incapable of elevation. Education is despised, or at least neglected, and heroic spirit is almost utterly extinguished. To remedy these defects would be an object worthy of serious attention. (Smith, 1978, p. 541)

Smith also analysed the influence of commerce on the manners of a people. He was convinced that introducing commerce to a country facilitated spreading of virtues of honesty and punctuality. He gave the example of the Dutch who “Of all the nations in Europe, the Dutch […] are the most faithful to their word”, which stems from not their national character but the development of commercialisation. Commerce forces people to be honest, a dishonest merchant will fail in the end.

When a person makes perhaps twenty contracts in a day, he cannot gain so much by endeavouring to impose on his neighbours, as the very appearance of a cheat would make him lose. When people seldom deal with one another, we find that they are somewhat disposed to cheat, because they can gain more by a smart trick than they can lose by the injury which it does their character. They whom we call politicians are not the most remarkable men in the world for probity and punctuality. Ambassadors from different nations are still less so […]. But if states were obliged to treat once or twice a day, as merchants do, it would be necessary to be more precise, in order to preserve their character. (Smith, 1978, pp. 538–539)

It does not mean, however, that Smith did not see the unethical practices of merchants. He wrote in *The Wealth of Nations* (1776/1954, Vol. 1, p. 127):

Our merchants and master-manufacturers complain much of the bad effects of high wages in raising the price, and thereby lessening the sale of their goods both at home and abroad. They say nothing concerning the bad effects of high profits. They are silent with regard to the pernicious effects of their own gains. They complain only of those of other people.

Smith believed that it is in the interest of merchants and manufacturers to limit competition, which contradicts the public interest because it serves only to increase their profits out of natural proportions at the cost of the rest of the society. Therefore, all regulations put forward by these classes should be thoroughly investigated with “the most suspicious attention”. It is because these are the classes “who have generally an interest to deceive and even to oppress the public, and
who accordingly have, upon many occasions, both deceived and oppressed it” (Smith, 1776/1954, Vol. 1, p. 328). He wrote about capital owners investing in the textile industry in a straightforward manner:

They are as intent to keep down the wages of their own weavers as the earnings of the poor spinners, and it is by no means for the benefit of the workman that they endeavour either to raise the price of the complete work or to lower that of the rude materials. It is the industry which is carried on for the benefit of the rich and the powerful that is principally encouraged by our mercantile system. That which is carried on for the benefit of the poor and the indigent is too often either neglected or oppressed. (Smith, 1776/1954, Vol. 2, p. 330)

Smith also presents a claim that agricultural work is better than most “mechanic trades”. He believes that the mind of a simple ploughman is “more used to considering various tasks”, is usually better developed than the mind of a manufacturing worker—a mechanic, who focuses mainly on performing one or two simple actions. In Book III, he claims that in Middle Ages and in modern times, European states supported the development of cities at the expense of the countryside, which was “in every respect contrary to the order of nature and reason”. He thought, “the interests, superstitions, laws and customs” caused it. His specific liking for agriculture is visible in many places in *The Wealth of Nations*. He believed that the property owners, farmers and agricultural workers paid the rising prices of guild privileges and the tariffs protecting local craft

They have commonly neither inclination nor fitness to enter into combinations; and the clamour and sophistry of merchants and manufacturers easily persuade them that the private interest of a part, and of a subordinate part of the society, is the general interest of the whole. (Smith, 1776/1954, Vol. 1, p. 168)

In a different part, Smith criticises landlords as vain egoists, acting upon the maxim: “Everything for us, nothing for the others”, who were willing to pay the price of annual expenses of a thousand people to buy a thing as petty as diamond shoe buckles.

We can see then that the principle of the priority of common good becomes a fundamental rule of Smith’s social philosophy, not only his economy. To do justice to the importance of this concept in Smith’s work is beyond the scope of this paper. In his own words, Smith (1776/1954, Vol. 2, p. 70) expressed, “the legislature, were it possible that its deliberations could be always directed, not by the clamorous importunity of partial interests, but by an extensive view of the general good.”

The mentioned principle is usually overshadowed by a traditionally exposed claim that the author of *The Wealth of Nations* based his economic theory on the assumption that *homo oeconomicus* is egoistic by nature. Moreover, the principle of sympathy, understood as natural human kindness is often excluded from the
readings of *The Theory of Moral Sentiments*. For the supporters of *Das Adam Smith Problem*, it is difficult to deal with the potential conflict between the assumptions upon which the two works were based (cf. e.g. Montes, 2003).

In conclusion, it should be added that Smith criticises such traits of individuals as wastefulness, profligacy, idleness. He thinks, however, that a country’s impoverishment is not caused by wastefulness or mismanagement of individuals but from wasting the public revenue and bad government. He praises the spending on durable goods but scorns individuals wasting money on direct consumption, which later leaves them with nothing, or on not important things, of which he judges most harshly accumulating dainty clothes. Spending money on truffles, „small ornaments for clothes and furniture, jewels, trinkets, often expose a character not only vain but also low and selfish” (Smith, 1776/1954, Vol. 1, p. 443).

In *The Theory of Moral Sentiments*, Smith claims that most people desire fame and fortune not because they want a comfortable life or happiness, but because they are vain. They want to improve their station in life. They want attention and want that others should serve on them. They desire sympathy and approvals that they can derive some satisfaction. A person of lower status has to work much harder and demonstrate his virtues and skills repeatedly. A wealthy person, on the other hand, cares only to shine at a ball, and considers his success in a love affair an achievement. In the courts, flattery is sometimes praised more highly than being useful. A wealthy individual rarely sees people of lower status as their fellow beings. This common tendency to look up to the rich and look down upon and ignore the poor, Smith calls, “the great and most universal cause of the corruption of our moral sentiments” (Smith, 1776/1954, Vol. 1, p. 87). An ambitious individual, willing to stand out, gain fame and respect has two paths to take: education and practising virtue or gaining wealth and social status. Choosing the latter exposes them to various dangers because the roads to wealth and virtue rarely meet.

**References**


