

## Adam Smith and the Theory Of Value: Chapter Six Considered

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Adam Smith enjoys a rather precarious position in the development of economic theory. On the one hand, he is recognized as the “Father” of the discipline (though not without progenitors—he's not the original Adam). At the same time, his work contains “dangerous” elements: one interpretation places Smith squarely in the line of descent that leads to Marx. The primary line of argument, however, purges Smith of dangerous thoughts, developing a lineage that runs from Smith to neoclassicism.

The major requirement if the prevailing argument is to hold is that a demonstration be erected that proves Smith either never held a labor-embodied theory of value, or, at a minimum, merely consigned this general point of view to the “early and rude” level of social development. If this end is not achieved, and if consistency is indeed a virtue, the ongoing attack on Marx must include an attack on the “Father” himself. Paul Douglas has indicated what such consistency must lead to:

There are, it seems to me, few more unfair instances in economic thought than the almost complete unanimity with which the English-speaking economists of the chair have heaped condemnation upon the overworked and poverty-stricken Marx, who worked under such great difficulties, and, save for the comments of Jevons and a few others, have heaped praises upon Smith and Ricardo. The failure was the failure not of one man but of a philosophy of value, and the roots of the ultimate contradiction made manifest to the world in the third volume of Das Kapital lie imbedded in the first volume of the Wealth of Nations (1928, p.95).

It has become generally accepted that Adam Smith abandoned a labor-embodied theory of value and argued a cost-of-production theory to explain value under capitalist exchange relations. In his *History of Economic Analysis*, Schumpeter states:

... in Book I, Chapter VI, A. Smith expressly states: Wages, profit, and rent are the three original sources of all revenue as well as of all exchangeable value. If words mean anything, this is conclusive. His theory of value was what later on came to be called a cost-of-production theory. This is indeed the opinion of many students (1961, p.309).

That Schumpeter's position is indeed that of convention can be illustrated by reference to textbook accounts, those great depositories of received (and conventional) doctrine:

The value of a commodity is the sum of the normal amounts payable to all the factors used in making it; hence, in the real world the natural price of an article is determined by money costs of production as made up of wages, rents, and profits, themselves the natural price of labor, land, and capital (Blaug 1962, p.41).

In the long run, then, the price of a commodity is determined solely by costs of production. The price of every commodity resolves itself into the sum of the natural rates of wages, profit and rent (Canterbery 1980, p.54).

But once capital comes to be employed in the productive process and land has become private property, the prices of goods resolve themselves into wages, profits, and rents. Thus Smith's labor theory of value becomes transformed into a cost-of-production theory (Spiegel 1971, pp.249-50).

Smith is rightly credited with his rejection of the labor theory of value. He banished it to that early and rude state of society which precedes both the accumulation of stock and the appropriation of land. Which value theory did he hold, then? His answer is found in what Schumpeter called by far the best piece of economic theory turned out by A. Smith . . . (a cost-of-production theory) (Brems 1986, p.71).

Even Dobb, at least in his later period, adopted this view of Smith's position on Value:

Thus we have in Smith a theory of price that can be characterised . . . as an Adding-up Theory—a summation (merely) of three primary components of price. It has alternatively been described as a simple Cost of Production Theory; in which guise it has been handed down through the nineteenth century and become known in textbooks of the subject (1973, p.46).

By way of a last word in support of this contention, *The New Palgrave*, perhaps the definitive statement on most topics, states the following:

According to Smith, when profit and rent make their appearance alongside the labourer's income, the above rule (beaver-deer)<sup>1</sup> is no longer applicable. The price of a commodity is then obtained by adding up its 'component parts': wage, profit and rent. These revenues, which Smith calls 'the three original sources . . . of all exchangeable value' enter into the 'natural price' of each commodity at their respective 'natural rates', such that the 'natural price itself varies with the natural rate of each of its component parts, of wages, profit and rent' (Vianello 1987, p.107).

Let us be very clear as to what the issue is. If Smith did hold a cost-of-production theory of value, then his value theory is fundamentally no different from at least one strain of neoclassicism. Basically, such a theory is equivalent to that of Marshall's long-run price determination (under constant returns to scale) where equilibrium prices will be determined by and are equal to the costs of producing the commodity in question.

I shall argue that Smith did hold a labor-embodied theory of value (though not without ambiguity or inconsistency); that, for Smith, labor was both the cause and measure of value; that the so-called cost-of-production theory was not an attempt to develop a different valuation approach suitable for exchange societies where property was privately held, but an argument pertaining to the distribution of value produced. I shall not debate the issue of the validity of a labor theory of value—that would take us far afield of this particular investigation. However, it will be pointed out as part of the conclusion what the practical results of the contending points of view are.

Lastly, by way of introduction, I shall not deal in any substantial way with Smith's labor-command theory of value. It is readily admitted that he did periodically slip into this theory of valuation. With the labor-command approach, Smith examined value from the exchange, rather than the production, point of view. Clearly, his labor-embodied theory took production at its starting point. (On this, see Marx 1969a, pp.75-7, *passim*; and Douglas, 1928, pp.88-95).<sup>2</sup> In passing, though, let me note that this approach can be construed as another supposed link to the neoclassical argument. In the standard approach to a labor-command theory, labor becomes a mere *numéraire*. As Schumpeter has pointed out, such a theory could just as readily be an "ox theory of value" as that of labor (1961, p.310). Given this, the command theory bears a similarity to that of Walras in which there

is no “cause” of value, merely a measure or *numéraire*. The basic difference, then, would be the choice of measure. At the same time, it must be observed that Smith did not choose “ox” for his measure, but continued to argue in terms of “labor.” If anything, his choice for a *numéraire* was “corn,” representing a surrogate for workers' subsistence. But, as this is not the issue addressed here (though see below), we shall move on, analyzing the question based, as it must be, on the textual context of *The Wealth of Nations*, with particular reference to Book I, Chapter VI—the point of departure for the cost-of-productionists.

### The General Point of View

In the opening sections of *The Wealth of Nations*, Smith is very clear as to how he perceives the economy of any society:

The annual labour of every nation is the fund which originally supplies it with all the necessaries and conveniences of life which it annually consumes, and which consist always either in the immediate produce of that labour, or in what is purchased with that produce from other nations.

The cause of this improvement (in social well-being) in the productive powers of labour, and the order, according to which its produce is naturally distributed among the different ranks and conditions of men in the society, make the subject of the First Book of this Inquiry (1937, pp.lvii, lviii).

There can be no mistake as to what Smith's perception was. The welfare of a nation was dependent upon its economic output. This output was the product of the social labor of that nation, working with the raw materials and machinery at its disposal. That is, labor is the cause or origin of the value of output. Further, in the distribution process, the various income shares represent output produced by labor.

Given this general perspective, then, the first step in the determination of value was the determination of the output that was to be exchanged. This output was nothing more than the labor embodied in production. This is unequivocally the first step in an analysis based upon a labor-embodied theory of value. Smith then proceeds to build upon this foundation in Book I, Chapter V.

In introducing this and the next two chapters, Smith tells us explicitly what he has in mind:

In order to investigate the principles which regulate the exchangeable value of commodities, I shall endeavour to shew, First, what is the real measure of this exchangeable value; or wherein consists the real price of all commodities. Secondly, what are the different parts of which this real price is composed or made up. And, lastly, what are the different circumstances which sometimes raise some or all of these different parts of price above, and sometimes sink them below their natural or ordinary rate; or, what are the causes which sometimes hinder the market price, that is, the actual price of commodities, from coinciding exactly with what may be called their natural price (pp.28-9).

The above statements are quite clear in their intent: Chapter V of Book I will tell us what Smith's theory of value is; Chapter VI will investigate the component parts of value. As Smith's theory of value hinges on these two chapters, it is necessary to engage in an analysis of both Smith and his interpreters on this ground.

### On Book I, Chapter V

Smith's basic theory of value is set forth in Chapter V of the first Book, entitled: “Of the Real and Nominal Price of Commodities or of Their Price in Labour, and The Price in

Money.” This heading should be a sufficiently large clue to the resolution of the issue. The first paragraph reads:

Every man is rich or poor according to the degree in which he can afford to enjoy the necessities, conveniences, and amusements of human life. But after the division of labour has once thoroughly taken place, it is but a very small part of these with which a man's own labour can supply him. The far greater part of them he must derive from the labour of other people, and he must be rich or poor according to the quantity of that labour which he can command, or which he can afford to purchase. The value of any commodity, therefore, to the person who possesses it, and who means not to use or consume it himself, but to exchange it for other commodities, is equal to the quantity of labour which it enables him to purchase or command. Labour, therefore, is the real measure of the exchangeable value of all commodities (p.30).

Though Smith alternates between a labor-embodied and labor-command theory of value in this paragraph, it is clear that labor is the standard by which value is to be determined. This is further confirmed in the third paragraph following:

But though labour be the real measure of the exchangeable value of all commodities, it is not that by which their value is commonly estimated. It is often difficult to ascertain the proportion between two different quantities of labour . . . . In exchanging indeed the different productions of different sorts of labour for one another, some allowance is commonly made for both. It is adjusted, however, not by an accurate measure, but by the higgling and bargaining of the market, according to that sort of rough equality which, though not exact, is sufficient for carrying on the business of common life (p.31).

Value is measured by the quantities of labor embodied in output. Price will deviate from value, though (under competitive conditions) not to the point where it is disruptive of the ordinary “business of common life.”

Essentially, the market translates the real, labor-embodied prices into those money prices which are observed in the exchange process, and which serve as conventional surrogates for the underlying values. In equilibrium, where prices equal values, the ratio of any two prices must equal the ratio of units of labor embodied in the commodities exchanged (as well as the ratio of units of labor commanded). Following Smith, “. . . the market price is . . . continually gravitating towards the natural price” (or price as measured by labor hours) (p.59).

Smith then proceeds to the argument that while labor is the actual measure of value, in a monetary economy money itself is the customary way of representing value, though the nominal prices themselves are adjusted on the basis of the labor expended in both the production of money and other commodities:

But when barter ceases, and money has become the common instrument of commerce, every particular commodity is more frequently exchanged for money than for any other commodity . . . . Hence it comes to pass, that the exchangeable value of every commodity is more frequently estimated by the quantity of money, than by the quantity either of labour or of any other commodity which can be had in exchange for it.

Gold and silver, however, like every other commodity, vary in their value, are sometimes cheaper and sometimes dearer, sometimes of easier and sometimes of more difficult purchase. . . . Labour alone, therefore, never varying in its own value<sup>3</sup> is alone the ultimate and real standard by which the value of all

commodities can at all times and places be estimated and compared. It is their real price; money is their nominal price only (pp.32-3).

And, following an analysis of rent based on a labor-embodied theory of value, Smith then states:

Labour, therefore, it appears evidently, is the only universal, as well as the only accurate measure of value, or the only standard by which we can compare the values of different commodities at all times and at all places (p.36).

Chapter V, then, is unambiguous, as least as far as the controversy surrounding the labor versus cost-of-production theories of value are concerned. Granting that there is some switching between a labor-embodied and labor-command theory, it is clear that Smith adopts a labor standard in his analysis of the valuation process. If we couple Chapter V to the Preface, Smith is reasonably explicit as to what he is arguing. We are told that labor is the “fund” which produces output, and, as its productive power increases, is the “cause” of all social improvement. This labor-produced value is then distributed among the “different ranks and conditions of men.” In a market or monetary (not “rude”) economy, prices reflect (though rarely equal) the labor required to produce the output exchanged.

If one proceeds through Smith’s argument beyond Chapter V, further evidence is provided to support a labor-embodied approach. Returning to the position first stated in his preface, he employs the labor-embodied theory to speak to distributional justice:

No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable. It is but equity, besides, that they who feed, cloath and lodge the whole body of the people, should have such a share of the produce of their own labour as to be themselves tolerably well fed, cloathed and lodged (p.79).

The consideration of these circumstances may, perhaps, in some measure explain to us why the real price both of the coarse and of the fine manufacture, was so much higher in those ancient, than it is in the present times. It cost a greater quantity of labour to bring the goods to market. When they were brought thither, therefore, they must have purchased or exchanged for the price of a greater quantity (p.246).

Smith again reiterates that, while labor produces all output (value), it receives only a niggardly share of that output: the remainder must go to those who do not contribute to the generation of value but who receive portions as distributive shares—profit, rent, etc. And, (real) price is determined by labor content only.

To such quotations, one should add the whole of Book II, Chapter III, “Of the Accumulation of Capital, or of Productive and Unproductive Labour.” Here Smith is abundantly clear that value is produced by labor only, and that all revenue (or income) produced by *productive* labor is shared among the various classes of society (including that portion of the working class termed “unproductive”).

There is one sort of labour which adds to the value of the subject upon which it is bestowed: there is another which has no such effect. . . . Thus the labour of a manufacturer adds . . . to the value of the materials which he works upon, that of his own maintenance, and of his master’s profit. . . . Though the manufacturer has his wages advanced to him by his master, he, in reality, costs him no expence, the value of those wages being generally restored, together with a profit, in the improved value of the subject upon which his labour is bestowed (p.314).

Both productive and unproductive labourers, and those who do not labour at all, are all equally maintained by the annual produce of the land and

the labour of the country. This produce. . . can never be infinite, but must have certain limits. According, therefore, as a smaller or greater proportion of it is in any one year employed in maintaining unproductive hands, the more in the one case and the less in the other will remain for the productive, and the next year's produce will be greater or smaller accordingly; the whole annual produce, if we except the spontaneous productions of the earth, being the effect of productive labour (p.315).

Observe that Smith is unambiguous here in specifying that productive labor *produces* value, including the profit that then covers the wages advanced by the capitalist; that *all* output (excluding the portion "spontaneously" produced by nature) is the result of productive labor. "Capital" certainly does make a contribution to output, but only through activating productive labor:

Parsimony, by increasing the fund which is destined for the maintenance of productive hands, tends to increase the number of those hands whose labour adds to the value of the subject on which it is bestowed. It tends therefore to increase the exchangeable value of the annual produce of the land and labour of the country. It puts into motion an additional quantity of industry, which gives an additional value to the annual produce (p.321).

What distinguishes a capitalist economy from that of the earlier "rude" organization is that land and "stock" have been privately appropriated. Hence, labor must be set in motion by those controlling such property, and no property owner would activate labor unless there were a benefit (profit or rent) in so doing. Owners then certainly have a claim on a portion of the output produced as it is their rights in property that allow such a claim. But it is still labor that "adds to the value of the subject upon which it is bestowed." (See, as well, page 348 in this regard.)

It is important to specify that Smith did not see labor as merely a measure of value (as *per* Schumpeter), even though he often refers to labor as such a measure. First, if labor were simply this, Smith could have chosen *any* physical economic variable to stand as a standard—one ox, one acre of land of specified fertility. He did not. Indeed, he specifically rejects gold and silver as such a measure. Further, as a measure of value merely represents a base from which *relative* value can be assigned, why would Smith (or any other economist) dwell on such a measure. It is sufficient to specify one's unit of account, then move on. But Smith returns to labor repeatedly, reminding the reader that the whole of the analytic scheme in the first Book rests on this standard.

I believe that Smith, writing in the 1700s, was less concerned with the controversies of the 1900s than in attempting to develop a general theory of the workings of a capitalist economy starting from an analysis of production. His use of the term "measure" should not be interpreted as one might today. If one examines the context of these passages, and places the Preface and Chapter V in the same general framework, one observes that Smith begins with the *production* of value as undertaken by labor; the exchange value of the output produced is represented by a quantity of labor that is its "real" (not nominal) value, and this labor then "measures" the value embodied in the commodity.

## **Chapter VI: Of the Component Parts of the Price of Commodities**

Having established a labor theory of value in Chapter V, and explaining the relationship between price and value, Smith then proceeds to examine the various constituent elements of price as representing the shares of income into which that price can be divided. Four citations indicate what Smith was addressing here.

Following the opening paragraph on the “early and rude state of society,” Smith states:

In this state of things, the whole produce of labour belongs to the labourer; and the quantity of labour commonly employed in acquiring or producing any commodity is the only circumstance which can regulate the quantity of labour which it ought commonly to purchase, command, or exchange for (pp.47-8).

Then, with “the accumulation of stock in the hands of particular persons” or private property in the means of production:

The value which the workmen add to the materials, therefore, resolves itself in this case into two parts of which the one pays their wages, the other the profits of their employer upon the whole stock of materials and wages which he advanced.

In this state of things, the whole produce of labour does not always belong to the labourer. He must in most cases share it with the owner of the stock which employs him. Neither is the quantity of labour commonly employed in acquiring or producing any commodity, the only circumstance which can regulate the quantity which it ought commonly to purchase, command, or exchange for. An additional quantity, it is evident, must be due for the profits of the stock which advanced the wages and furnished the materials of that labour (pp.48-9).

And:

As soon as the land of any country has all become private property, the landlords, like all other men, love to reap where they never sowed, and demand a rent even for its natural produce. The wood of the forest, the grass of the field, and all the natural fruits of the earth, which, when land was in common, cost the labourer only the trouble of gathering them, come, even to him, to have an additional price fixed upon them. He must give up to the landlord a portion of what his labour either collects or produces. This portion, or what comes to the same thing, the price of this portion, constitutes the rent of land and in the price of the greater part of commodities makes a third component part (p.49).

What Smith is addressing is not the production of value (or output), but its distribution. That is, any price which represents value can be seen as amounting to the portions of that price which constitute the income shares of workers, capitalist, and landlords. Price, or value, then, is not the result of adding up the costs of production (which, of course, would then require an explanation of those costs independent of the price of the commodity), but rather the total of the shares must equal price. Hence, at the aggregate level, the sum of the prices representing the sum of the commodities exchanged must equal the sum of the various income shares distributed. Or, the value of output must equal total income.

That Smith *is* addressing the distribution of the value produced by labor is made clear by the manner in which the questions posed are addressed: “The value which the workmen add . . . resolves itself into two parts . . .”: “(The labourer) must . . . share it with the owner . . .” Here (and elsewhere) Smith locates the source of value or output in the labor expended in production. With private property, the whole of output cannot be returned to the labor that produced it. Some portion must be given over to those who own capital or land—value must be *shared*.

Smith’s position becomes even clearer if we turn to Chapter VIII, “Of the Wages of Labour.” Here, Smith discusses rents and profits as “*deductions*” from the value produced by labor (p.65). These deductions are the consequence of the appropriation of land and the accumulation of “stock.” Landlords demand “. . . a share of almost all the produce which

the labourer can . . . raise . . . from (land),” and the capitalist “. . . shares in the produce of their labour, or in the value which (labor) adds to the value upon which it is bestowed; and in this share consists his profit” (*ibid.*).

Land exists prior to appropriation and was certainly an input in the production process in the “early and rude” stage of development—and many, if not most, historians of economic thought agree that Smith argued a labor-embodied theory of value as underlying this stage of history. When land becomes privatized, ownership does nothing to affect the nature of production: if labor produced all value prior to appropriation, it continues to do so after appropriation. Landlords, however, are now in a position to claim income—a “share” of output—solely on the basis of that ownership, reaping where they do not sow.

It is noted, however, that in the above quotation from page 49 of *The Wealth of Nations*, Smith does commit an error which *could* be interpreted as a cost-of-production theory of value. After arguing that the introduction of private property mandates that the “whole produce of labour does not always belong to the labourer,” and that the labourer must “share it with the owner of stock,” he then goes on to state that profits represent an “additional quantity” beyond that produced by labor.

That this indeed is an error (or an internally inconsistent proposition) can be demonstrated: if output is the result of labor (the starting proposition), then it can only be “shared” among the various classes of society. If profits were an “additional” quantity, added to the value produced by labor (proposition two), then this “tacked on” income *could not* represent any additional output. The two sides of the equation simply do not add up—the sum of the incomes would be greater than the sum of the output produced.

Now, if capital does contribute to the production of value, then profit—as capital’s reward—*would* represent an increase in value and *not* a deduction from the value created by labor. A cost-of-production theory would then be consistent with Smith’s general approach.

There are two problems with this standard view, however. First, Smith identifies capital as private property. “Tools,” like land, existed prior to privatization and the same argument would hold as with that regarding land (above). Just because “. . . workers stand in need of a master to advance them the materials of their work, and their wages . . . till it is completed” (p.65) does not change the technical nature of production. In the “early and rude” stage, labor had to eat previously produced food and used tools produced in past production periods in order to produce current output. What changes is the social nature of production, where capital, or privately appropriated tools, force a separation of labor and previously produced output, allowing capitalists to “share in the produce of their labour. . .”

The second problem is theoretical. From a cost-of-production perspective, capital and land must increase the value of output produced above that which labor alone could contribute. (Were this the case, one could then relate the increase in value to the respective contributions of the various inputs and argue a productivity theory of distribution.)

It is quite true that capital (here seen as machines) does allow an increase in the *total* values created (GDP), but only through the increase in the productivity of labor. And, as Smith makes clear, as the productivity of labor increases, the value of a commodity falls rather than increases given that the labor time required to produce a commodity has been reduced:

The produce of labour constitutes the natural recompense or wages of labour. In that original state of things, which precedes both the appropriation of land and the accumulation of stock, the whole produce of labour belongs to the labourer.



Had this state continued, the wages of labour would have augmented with all those improvements in its productive powers, to which the division of labour gives occasion. All things would gradually have become cheaper. They would have been produced by a smaller quantity of labour . . . (p.64).

Smith's position on capital reducing unit value is taken up periodically *throughout The Wealth of Nations*. For instance:

Both in the coarse and in the fine woollen manufacture, the machinery employed was much more imperfect in those ancient, than it is in the present times. It has since received three very capital improvements . . .

The consideration of these circumstances may, perhaps, in some measure explain to us why the real price both of the coarse and the fine manufacture, was so much higher in those ancient, than in the present times. It cost a greater quantity of labour to bring the goods to market. When they were brought thither, therefore, they must have purchased or exchanged for the price of a greater quantity (p.246).

If profit (and rent) were additional costs, value would increase with the application of capital. But value falls accordingly. And the reduction in price that follows the reduction in value cannot then be representative of an increase in cost (value) associated with the increase in capital.

In any case, in trying to make this point clear, Smith states:

The real value of all the different component parts of price, it must be observed, is measured by the quantity of labour which they can each of them, purchase or command. Labour measures the value not only of that part of price which resolves itself into labour, but of that which resolves itself into rent, and of that which resolves itself into profit (p.50).

However, it is noted that in typical Smithian fashion, following the above statement, Smith then proceeds to add a point of confusion in which the labor theory of value as applied to distribution is co-mingled with a cost-of-production theory, as in the quote critiqued above:

As the price or exchangeable value of every particular commodity, taken separately, resolves itself into some one or other, or all of those three parts; so that of all the commodities which compose the whole annual produce of the labour of every country, taken complexly, must resolve itself into the same three parts, and be parcelled out among different inhabitants of the country, either as the wages of their labour, the profits of their stock, or the rent of their land. The whole of what is annually either collected or produced by the labour of every society, or what comes to the same thing, the whole price of it, is in this manner originally distributed among some of its different members. Wages, profit, and rent are the three original sources of all revenue as well as of all exchangeable value. All other revenue is ultimately derived from some one or other of these (p.52).

Here, Smith contradicts himself. He tells us that value (or price) must "resolve itself" into wages, profits, and rents. But, the value itself was produced by labor. While wages, profits, and rent are clearly the "original sources of all revenues" or *income*, they cannot be the source of exchange value—if labor is.

As this last citation is ambiguous in its content, and also clearly runs counter to his previous argument, it should be reasonably seen as a slip—a slip which the cost-of-production adherents have seized upon as representative of Smith's general position (as in Schumpeter's position above).<sup>4</sup>

## The Position of the Immediate Post-Smithian Critics

It is of some interest that the anti-labor theorists of the fifty-year period following Smith were not of the same mind as the modern cost-of-productionists. During this period, the political contests waged were both more open and more trenchant than in the present period, and those forces representing the anti-labor theory position were forced to deal with their opponents in a more forthright fashion (see Henry 1990, pp.84-173). Say, for example, argued that:

To the labour of man alone he (Smith) ascribes the power of producing values. This is an error . . . From this error Smith has drawn the false conclusion, that all values produced represent pre-exerted human labour or industry . . . from which position he infers a second consequence equally erroneous, *viz.* that labour is the sole measure of wealth, or of value produced (Say 1971, pp.XL, 16).

And Lauderdale, in describing how economics had changed since the time of Smith, stated:

Labour is no longer regarded as a measure of value . . . It is, by all, admitted, that capital derives its profits, either by supplanting a portion of labour . . . or, from its performing a portion of labour which is beyond the reach of the personal exertion of man . . . (Maitland 1966, pp.xx-xxi).

In the post-Ricardian period, following the appearance of the so-called “Ricardian Socialists” who were recognized as linked to Smith through their sometimes use of a labor theory of value, we find a renewed attack on the labor theory of value. George Scrope is representative of this position:

Smith and his followers have insisted much on everything having a *real* value, which they define to consist of the quantity of *labour* required to produce it; and they accordingly call labour the natural standard or measure of value. . .

It has, however, been urged by these writers that the exchangeable value of anything will always depend on the quantity of labour necessary to procure or produce it, and on this ground it is proposed as the best measure of the value which it composes. . . . (Scrope 1969, pp.166-7).

These economists, representative of the main positions of their times, clearly did not hold that Smith held a cost-of-production theory. Rather, they were unanimous in arguing that a labor-embodied theory of value was the basis of Smith's general theory. Given the political ramifications of the two theories, it would be reasonable to assume that these economists were much more attuned to the sensibilities of the day: that is, given the ramifications of a labor theory of value, had they really believed that Smith held a cost-of-production theory, they would have “corrected” his “dangerous” view accordingly.

## Conclusion

Adam Smith held a labor theory of value, not only in the context of an “early and rude” society, but as an explanatory theoretical tool in his examination of an advanced (for his period) capitalist organization. To be sure, he did alternate between a labor-embodied and labor-command approach. But, as he never specified anything but labor as a standard in his command theory (no oxen or any other commodity is brought forward as an alternative measuring rod), one can reasonably argue that Smith was (generally) clear as to what his general point of view was.

No cost-of-production theory of value exists in Smith. Commentators have substituted Smith's first approximation of a theory of distribution for his theory of value.

Succinctly, in *The Wealth of Nations*, value (or output) produced by labor must be divided among the three classes of society which own the various factors of production. As the sum of wages, profits, and rents (plus peripheral payments) must equal the sum of output generated, than value can be viewed as the “adding up” of the various costs of production received as distributive shares. But these costs are determined and measured by value (labor); they are not the basis of value.

As Smith is reasonably clear on these matters, why is it that the cost-of-production argument has come to be the standard position regarding Smith's value theory? One can speculate of course: failure to grasp the classical approach to economic theory and analysis; the attempt to read pseudo-neoclassical argumentation in the words of the father of the discipline (witness the ever-present claim that if only Smith had understood *marginal* utility he would have “solved” the diamond-water paradox); failure to read original sources, instead relying on secondary sources which mistakenly had made the cost-of-production argument initially; technical errors in Smith's manuscript, possibly the result of it being dictated. To this listing, one can add a multitude of other explanations.

One argument that does place the issue into a fundamental framework concerns the general direction in which each of the theories of value leads. This is stated quite succinctly by Rima and is implicit in most treatments of the question:

What is the significance of Smith's explanation of natural price for the labor theory of value? Smith nowhere denies the right of the owner of stock to receive profit or of the landlord to receive rent. On the contrary, he regards the existence of these shares as being ‘natural’ once ‘that early and rude state of society’ (before the advent of privately owned land and accumulated stock) is past. What this implies from the standpoint of the value problem is that the cost of production tends to be the long-run determinant of value. Smith does not, of course, say this. Nowhere is the validity of the labor theory of value specifically limited to a primitive society. The dilemma thus becomes obvious. Does labor create all value, so that the deduction of a share for the landlord and the owner of stock represents exploitation of what rightfully belongs to the worker? It never occurred to Smith to reason along these lines, for his was a beneficent society in which there is no dichotomy of class interests. But the door to a theory of class conflict was opened to those who, like Karl Marx, would later argue that the deduction of rent and profit from the total revenue of the sale of a commodity necessarily meant a discrepancy between its labor cost and its labor command (Rima 1986, pp.86-7).

I have no hesitation in agreeing with Rima that this is most likely the central concern in the matter. A labor theory of value does lead to Marx by way of Ricardo, and does generate the eventual Marxist conclusions. Hence, from this point of view, Smith is a forerunner of Marx. And this does not sit well with those of the standard neoclassical mode who view Smith as *their* ancestor. On the other hand, if a case can be made for the cost-of-production argument, Smith can be equated with Marshall and his (long-run) cost-of-production approach to normal price. Modern theory, then, can trace its origins to Smith, and Marx (along with Ricardo) can be treated as deviants.

But what was Marx's position on this question?

... instead of resolving exchange-value into wages, profit and rent, he declares these to be the elements forming exchange-value, he makes them into independent exchange-values that form the exchange-value of the product; he constructs the exchange-value of the commodity from the values of wages, profit and rent, which are determined independently and separately. Instead of having their source in value, they become the source of value (1969b, p.217).

It must first be remembered that Marx's argument was that, in the main, Smith did hold a labor-embodied theory of value which became apparent whenever Smith analyzed the generation and distribution of surplus value. However, Marx argued that Smith's inconsistencies (expected during this period of the development of economics) led him at several points to the cost-of-production theory. (See Marx 1969b, pp.69-97.) For Marx, the cost-of-production statement of Chapter VI was an unfortunate error that ran counter to Smith's prevailing position. I think that Marx himself erred in this judgment. To be sure, Smith's statement as it stands is in error and does run counter to his prevailing view. Yet to state, as did Marx, that Smith *ended* with this position is simply incorrect. If that were the case, Smith would have continued his analysis with this (cost-of-production) theory of value as his foundation. He did not. Smith (or his secretary) simply erred or incorrectly formulated what he wanted to say. And Marx erred in this specific part of his interpretation of Smith.

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## Notes

<sup>1</sup> A reference to the “early and rude” stage prior to the appropriation of land and the accumulation of capital when commodities exchanged precisely at their labor-time values.

<sup>2</sup> Hans Jensen, in his critique of a previous draft of this paper, suggests that what Smith was really driving at with his labor-command approach was the accumulation of capital. Under “early and rude” conditions, the value which labor commands must be equal to the value which labor embodies in goods. Under conditions of privately held means of production, labor can command only a portion of what it embodies: profits and rents form the other constituent elements which command the remainder of the embodied labor. Profits, then, determine the amount of productive labor (that used to produce surplus in the next period) that capitalists can employ, and this determines the rate of growth. Hence, the labor-commanded approach is really concerned with the distribution of value, with particular emphasis placed on the share of total social labor commanded by this class.

I find this suggestion both insightful and intriguing, though, as it strays from the central point of this essay, it will not be pursued herein.

<sup>3</sup> Here Smith commits a slip, so common in his book. While labor, measured in “hours,” can certainly be viewed as invariant within a period of time in a given technological environment, it is not true that labor does not vary in its own value over extended periods of time accompanied by technological change. An “hour” of labor will be greater or less given the level of technology with which it produces. However, within a reasonable period of time, an hour of labor can be theoretically viewed as a constant.

<sup>4</sup> It should be noted that in this “slip,” Smith speaks of “exchangeable value.” Usually, when Smith is discussing *value*, he specifies *real* exchangeable value; nominal or market prices are usually referred to as exchangeable value only.

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