Chapter 1: It All Started with Adam

1776, a Prophetic Year
- The Enlightenment period came about, along with America’s Declaration of Independence, and the idea of “life, liberty, and the pursuit of happiness” as inalienable rights

A Monumental Book Appears
- March 9, 1776 – An Inquiry into the Nature and Cases of the Wealth of Nations by Adam Smith is published in London
- It was a declaration of economic independence promising a universal formula for prosperity for even the common man.

The Importance of the Enlightenment
- History of the Decline and Fall of the Roman Empire by Edward Gibbon is also published in 1776.
- Gibbon was an advocate of the Enlightenment as well, having faith in science, reason, and economic individualism.

The Rumblings of Economic Progress
- In the early 1800s (a few years after the publication of The Wealth of Nations), the industrial revolution began along with the rise of real wages and the standard of living.

Advocate for the Common Man
- The British economist, Alfred Marshall, called economics the study of “the ordinary business of life.”
- Adam Smith assured that his model for economic success would result in “universal opulence” for even the lowest ranked people, for his target audience was the average citizens who suffered the most in the economic cycle of long hours and subsistence wages

Adam Smith Faces a Major Obstacle
- Little progress had been achieved over the centuries because of the entrenched idea of mercantilism.
- He wanted to not only educate, but to persuade, the legislators and other mercantilists toward the real source of wealth and economic growth.

The Appeal of Mercantilism
- It was assumed that wealth and power could only be gained at the expense of other nations. “Wealth was therefore based on seizure and exploitation.”
- “The great affair, we always find, is to get money [i.e. gold and silver].”

Smith Denounces Trade Barriers
- Smith thought it “absurd” to have barriers on trade when some countries had the clear “natural advantage” to produce goods.
- He believed that since the mercantile system did not benefit the consumer, it was “antigrowth and shortsighted.”
- “If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them.”

Real Source of Wealth Revealed
Smith argued that the keys to the “wealth of nations” were production and exchange, not just the acquisition of gold and silver. Wealth should be measured according to how well people are lodged, clothed, and fed.

**Smith Discovers the Key to Prosperity**
- Give people their economic freedom!
- He encouraged the free movement of labor, capital, money and goods, without the interference of the state.
- Natural liberty is the right to buy goods from any source (domestic or foreign) without the restraints of tariffs or import quotas. It is also the right to charge whatever wage the market may bear as well as the right to save, invest, and accumulate capital.

**Adam Smith’s Crowned Jewel**
- George Stigler called Smith’s model the “crown jewel,” that an economic system that allows men and women to pursue their own self interest through “natural liberty” and competition would be prosperous.
- Eliminating restrictions on imports, labor, and prices meant that prosperity could be maximized through lower prices, higher wages, and better products.

**Smith Identifies Three Ingredients**
- Freedom – individuals have the right to produce and exchange products, labor, and capital as they see fit (self-interest)
- Competition – individuals have the right to compete in the production and exchange of goods
- Justice – the actions of individuals must be just and honest, according to the rules of society

**The Benefits of the Invisible Hand**
- “The invisible hand” – the symbol of the stable workings of the market economy when individuals pursue their self-interest

**Does Adam Smith Condone Egotism and Greed?**
- Self-interest does not mean ignoring the needs of others – both the buy and the seller benefit from every voluntary transaction.
- “It is not from the benevolence of the butcher, the brewer, and the baker, that we expect our dinner, but from their regard to their own interest” (pg. 24).
- Because he was also a professor of moral philosophy, Smith felt a good moral climate and a legal system would benefit economic growth.

**How Monopoly Hurts the Market System**
- Competition means lower prices and more money to buy other goods, which in turn means more jobs and a higher standard of living.

**Adam Smith Favors a Strong but Limited Government**
- “Little else is required to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice.”

**Smith Endorses Sound Money and the Gold Standard**
- Although he was against the idea that gold and silver alone constituted a country’s wealth, he did favor a stable monetary system based on gold and silver as well as supported the doctrine of free banking.

**Adam Smith and the Age of Economists**
- Smith was not perfect, and in later chapters, his theories will be amended and critiqued.