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by

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1. INTRODUCTION

It is widely recognized that the development of Ricardo's theory of profit sterns from Ricardo's 'dissatisfaction' with Smith's alternative theory running in terms of the 'competition of capitals'. This theory is generally known as the 'competition-of-capitals doctrine'. Much research has been done in recent years both on Ricardo's 'struggle of escape' from this doctrine and on the consistency of the analytical results of this escape. The focus of attention, however, has been mostly centered on Ricardo's alternative theory. This was developed first in his *Essay on Profits* (1815), where it took the elementary farm of a 'com-ratio theory of profits', and later on in the *Principles* (1821), where it took the more advanced form of the 'labour embodied theory of profits'.

The purpose of this chapter is to reconstruct Smith's (1776 [1976]) competition-of-capitals doctrine. This reconstruction, however, is not intended to provide a faithful assembly of what Smith actually wrote or a 'rational' view of what he must have thought in this connection. Rather, it is to extract from his faulty exposition and with the benefit of hindsight what is necessary to make Smith's doctrine consistent with his system of thought and vision of the future in order to determine whether, or to what extent, Ricardo's dissatisfaction is justified. This reconstruction will be based on the fragmentary statements by which the doctrine is presented in the *Wealth of Nations* and will try to highlight not only some of the ambiguities incorporated in these statements but also the links between these statements and other crucial parts of Smith's system of thought. These links, it will be argued, involve the wage-profit relationship.

This relationship is commonly traced to Ricardo' s *Principles* where it is used in support of Ricardo's theory of distribution. But the wage-profit relationship was first recognized and is extensively used in the *Wealth of Nations.* The role it plays in Smith's work, however, differs greatly from that in Ricardo's. Not only is Smith's relationship put forward in the context of that competition-of-capitals doctrine from which Ricardo endeavoured to escape, but this doctrine is also coherent with that part of Smith's theory of value which was rejected by Ricardo. Smith' s theory of value, however, is not the only framework in which the competition-of-capitals doctrine finds its proper place. Another framework is Smith's theory of capital. This theory was never rejected and, indeed, was instead defended by Ricardo on many controversial points.

Our reconstruction of the doctrine will run as follows. Section 3.2 presents the main fragments of the doctrine to be found in the *Wealth of Nations.* Section 3.3 examines the main ambiguities incorporated in these fragments. Section 3.4 locates the analytical foundations of the doctrine in Smith's theory of value and, particularly, in the principle of demand and supply in so far as it is part of this theory. These foundations are discussed in Sections 3.5 and 3.6 in the light of some clarifications introduced by Malthus and Senior. Section 3.7 shifts the focus of attention to the theory of capital and to the role played by the accumulation of capital in making the wage-profit relationship work in practice. This relationship, it will be argued in this section, is the link by which the competition-of-capitals doctrine interacts with Smith's theory of value as labour commanded, on the one hand, and with Smith' s theory of capital as command of productive labour, on the other. Section 3.8 is concerned with the sustainability of this link as the accumulation of capital proceeds in time. Some conclusions are drawn in Section 3.9.

2. THREE FRAGMENTS OF TRE DOCTRINE

Of the two theories which support Smith's competition-of-capitals doctrine one (the theory of value) eventually deals with the question concerning the commodity in which a variation in the 'exchangeable value' (from now onwards: e-value) originates while the other (the theory of capital) culminates in the analysis of the forces that account for a rise in the natural e-value of labour (natural wages). We will see below how these questions are instrumental to the conclusion of the doctrine. For now it is enough to note that Smith, while failing to argue how these questions relate to the doctrine, presents this doctrine in some passages so unconnected with, or so distant from, each other that it is either hard to take it as a doctrine or it is nearly impossible to discern the crucial role it plays in Smith's system of thought.

One of these fragments is found in Smith' s chapter on wages and is focused on the 'natural collusion' of masters to prevent a rise of wages:

“When in any country the demand far those who live by wages, labourers, journeymen, servants of every kind, is continually increasing; when every year furnishes employment for a greater number than had been employed the year before, the workmen have no occasion to combine in order to raise their wages. The scarcity of hands occasions a competition among masters, who bid against one another, in order to get work and thus voluntarily break through the natural combination of masters not to raise wages” *(Wealth,* Book I, Chapter VIII, p. 86)

Another fragment is found right at the beginning of Smith' s chapter on profits and focuses on the 'increasing or declining state of the wealth of the society':

“The rise and fall in the profits of stock depend upon the same causes with the rise and fall in the wages of labour, the increasing or declining state of the wealth of the society; but those causes affect the one and the other very differently. The increase of stock, which raises wages, tends to lower profit. When the stocks of many rich merchants are turned into the same trade, their mutual competition naturally tends to lower its profit; and when there is a like increase of stock in all the different trades carried on in the same society, the same competition must produce the same effect in them all” *(Wealth,* Book I, Chapter IX, p. 105)

Final!y, a third fragment qualifies the fall of profits in particular sectors ('into the same trade') and in the economy as a whole ('in any country') by focusing on what happens 'at both ends' of the subtraction by which profits are calculated:

“As capitals increase in any country, the profits which can be made by employing them necessarily diminish. It becomes gradually more and more difficult to find within the country a profitable method of employing any new capital. There arises in consequence a competition between different capitals, the owner of one endeavouring to get possession of that employment which is occupied by another. But upon most occasions he can hope to justle that other out of this employment, by no other means but by dealing upon more reasonable terms. Re must not only sell what he deals in somewhat cheaper, but in order to get it to sell, he must sometimes too buy it dearer. The demand for productive labour, by the increase of the funds which are destined for maintaining it, grows every day greater and greater. Labourers easily find employment, but the owners of capitals find it difficult to get labourers to employ. Their competition raises the wages of labour, and sinks the profits of stock” *(Wealth,* Book II, Chapter *N,* pp. 352-3).

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