

AN ANALYSIS OF ADAM SMITH'S THEORY OF CHARITY AND THE PROBLEMS OF THE POOR

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INTRODUCTION

A well-established literature recognizes Adam Smith's concern with issues of distributive economic justice [Winch, 1978, 98-9; Heilbroner, 1982; Young and Gordon, 1996], particularly the plight of the poor [Himmelfarb, 1983, 46-62], and some related research into how Smith's thought might justify a supportive role for the state in providing assistance to the poor [Baum, 1992]. However, the existing literature has failed to analyze the potential role of private charity in addressing the problem of poverty using Smith's writings as a foundation. As a result, the case for government intervention on behalf of the poor within the context of Smith's thought has not been fully explored. This paper addresses this shortcoming by examining Smith's theory of charity as it relates to the poor. Taken as a whole, Smith's writings reveal a complex theory of charity which allows for both self-regarding and altruistic motives of donors, assigns a prominent role to recipient behavior as a determinant of charitable giving, and recognizes psychological, ethical, historical, social, as well as economic factors influencing the nature and level of charitable activity.

In *The Theory of Moral Sentiments*, (hereafter *TMS*) Smith often speaks of the virtue of beneficence (which includes acts of charity, kindness, love, friendship and the like), but this virtue has received comparatively little attention among economists, evidently due to two reasons.¹ First, the core theoretical argument in *The Wealth of Nations* (hereafter *WN*) would appear to be that economic altruism is largely unnecessary in a competitive market system inhabited by just and prudent individuals. Second, beneficence is described by Smith in *TMS* as "the ornament which embellishes" society rather than being a virtue essential to social order or economic growth [(1759) 1976, 78]. The comparative neglect of beneficent acts such as charitable giving is not entirely justified, however, even within the context of Smith's own thought. As argued elsewhere [Baum, 1992], Smith was concerned about imbalances of economic power prejudicial to the poor created by the mercantilist system which, he argued, largely benefitted the capitalist class of merchants and manufacturers. Reinforcing this perspective is the fact that Smith emphatically declared that the "obvious and simple system of natural liberty" which he advocated in *WN* was a utopian vision which "not only the prejudices of the publick, but what is more unconquerable, the private interests of many individuals, irresistibly oppose" [*WN*, 687, 471]. The issue of charitable giving to benefit the poor is therefore highly relevant in a "second best" world created by rent-seeking capitalists or other market failures.

It is notable that Smith was not entirely satisfied with relying on markets to provide economic support to the poor as evidenced by his preference for a modified version of the government supported Scottish educational system over the strictly private charity system of education then in existence in England [Muller, 1993, 151].² Nevertheless, Smith was mostly silent on the issue of government intervention on behalf of the poor. One reason for Smith's reticence may have stemmed from his view that many government officials were incompetent or corrupt [Freeman, 1969], but any proclivity toward vice or inefficiency on the part of government naturally needs to be weighed against the possible imperfections of markets (philanthropic or otherwise) in directing resources to the poor. It is well-known that in order for resources to be allocated efficiently in a private market setting, certain conditions must be satisfied including free entry into the market, complete and accurate information by the market participants and the absence of external effects (unless there is a mechanism for internalizing those externalities). It is argued in this paper that the modern welfare-theoretic case for government intervention to assist the poor is provisionally supported by two prominent ideas regarding human psychology embedded in *TMS* which create allocative inefficiencies. First, the poor have a tendency to conceal their condition from the wealthy due to a sense of personal shame and fear of social disapprobation. This concealment contributes to the physical and psychological alienation of the poor from wealthier individuals, implying high transaction costs between the poor and their potential benefactors and a violation of the perfect information requirement for the efficient operation of private charity markets. Second, positive external effects may be generated by a charitable act because, according to Smith, third parties naturally approve of actions which express and promote benevolent feelings. This may result in a misallocation of aid to the poor depending on how much social approval is appropriated by the donor. The case for government intervention on allocative efficiency grounds is provisional because inefficiencies in the market provision of aid to the poor must be weighed against the inefficiencies associated with government redistribution [Buchanan, Tollison and Tullock, 1980; Mueller, 1989, 326-37] in order to determine the appropriate institutional response to the problem of poverty [James and Rose-Ackerman, 1986; Weisbrod 1988]. It is also argued that Smith's moral philosophy — in particular, his concepts of propriety and merit — further informs the public versus private charity debate.

The paper is organized as follows. The next section uses *TMS* to unpackage Smith's theory of charity and establishes a rationale for the existence of private charity markets for the poor within the context of Smith's writings. Next, sources of private charity market failure in Smith's theory are identified and the modern welfare-theoretic case for government intervention to assist the poor is reexamined. Finally, the broader historical question of the possibilities for economic altruism in a commercial society from Smith's perspective is considered. The last section provides some concluding remarks.

SMITH'S THEORY OF CHARITY

In *TMS*, Smith dryly observed that "[w]e are not ready to suspect any person of being defective in selfishness" [(1759) 1976, 304]. However, in his famous opening passage to *TMS*, Smith explicitly recognized the potential for acts of individual charity:

How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it. [*ibid.*, 9]

Smith here acknowledges self-regarding motives of personal utility as a possible rationale for caring about the happiness of others ("though he derives nothing from it except the pleasure of seeing it"), but certainly does not rule out other-regarding impulses of benevolence or, more broadly, an altruistic sense of duty as alternative reasons for caring about others.³ Smith's altruistic theory of charity is rooted in a human capacity for "fellow-feeling" [*ibid.*, 10]. Although fellow-feeling is often sparked by an instinctive emotional response, it develops more generally from an ability to imagine how one would feel *if* placed in another person's circumstance. Reason is then applied to determine if the emotions being expressed by the other person are warranted by the conditions. The greater the correspondence between our own imagined response and the actual response of another, the more perfect our "sympathy", a term Smith used in a broad way "to denote our fellow-feeling with any passion whatever" [*ibid.*, 10]. Endowed with these conceptual and rational faculties, the range of human sympathy is potentially greater and more elastic than within other species of animals whose fellow-feelings are more narrowly rooted in instinct. Thus, in the theoretical extreme, Smith spoke of the possibility of "universal benevolence" [*ibid.*, 235-37]; in practice, however, Smith observed that benevolent feelings were an inverse function of physical and social distances between people and this implied that benevolence, by itself, was inadequate for explaining human charity on a very large scale (mainly confined to activities within the family unit and therefore akin to the behavior of other animals).

Instead, the altruistic dimension of Smith's theory of charity pivots on the development of the virtue of self-command. In general, self-command is the ability to govern any type of passion [*ibid.*, 23-25]; however, in terms of altruistic charitable behavior, it refers to the ability to control or moderate selfish desires. Without such restraint, benevolent or humanistic feelings would typically conflict with and be dominated by narrow self-interest and therefore might never develop into positive acts of kindness. Initially, Smith provides grounds for optimism regarding the co-existence of benevolence and self-command within an individual by arguing that both are rooted in a "sensibility to the feelings of others" and therefore "[t]he man of the most exquisite humanity, is naturally the most capable of acquiring the highest degree of self-command" [*ibid.*, 152]. However, in practice Smith observed that "the situations in

which the gentle virtue of humanity can be most happily cultivated, are by no means the same with those which are best fitted for forming the austere virtue of self-command" [*ibid.*, 153]. The conditions conducive to nurturing feelings of benevolence (e.g., the personal ease and security provided by wealth, leisure and public order) are precisely the conditions opposed to the production of self-command, the latter relying on situations of adversity and hardship (e.g., competition, war, misfortune and destitution) to teach the self-sacrifices required for overcoming difficulty [*ibid.*, 204-05].

How, then, does Smith explain the emergence of self-command? Self-command is partly a product of an endogenous process of learning to view one's own behavior through the eyes of actual spectators in order to gain their praise. In this respect, Smith emphasized the early influence of a person's family and, later in life, the "bustle and business of the world" as "the great school of self-command" [*ibid.*, 146]. But Smith further argued that self-command is more powerfully rooted in a sense of duty which relies not upon actual spectators, but an inner, imaginary, "impartial" spectator to correct for "the natural misrepresentations of self-love" [*ibid.*, 137]. It is in Part III of *TMS* that Smith addresses the origins of personal duty and poses the question central to any theory of altruism:

When our passive feelings are almost always so sordid and so selfish, how comes it that our active principles should often be so generous and so noble? When we are always so much more deeply affected by whatever concerns ourselves, than by whatever concerns other men; what is it which prompts the generous, upon all occasions, and the mean upon many, to sacrifice their own interests to the greater interests of others? [*ibid.*, 137]

Smith's answer alludes to a self-respect which is decidedly more Stoic than Christian:

It is not the love of our neighbor, it is not the love of mankind, which upon many occasions prompts us to the practice of those divine virtues. It is a stronger love, a more powerful affection, which generally takes place upon such occasions; the love of what is honorable and noble, of the grandeur, and dignity, and superiority of our own characters. [*ibid.*, 137]

In the virtuous person, the desire to be praiseworthy supersedes the desire to be praised and whether it is praiseworthy to act altruistically is determined by "the eye of [the] impartial spectator ... who shows us the propriety of resigning the greatest interests of our own, for the yet greater interests of others" [*ibid.*, 137]. Adopting the perspective of the impartial spectator requires a measure of self-denial, and it is this which allows humanitarian motives to become active.⁴ In fact, Smith is very critical of what he calls "indolent benevolence", a phrase he uses to denote a kind of latent humanitarian virtue that will not flourish without some measure of self-restraint [*ibid.*, 106]. Along these same lines, Smith draws an important distinction between humanity and generosity:

Generosity is different from humanity ... Humanity consists merely in the exquisite fellow-feeling which the spectator entertains with the sentiments of the persons principally concerned ... The most humane actions require no self-denial, no self-command, no great exertion of the sense of propriety ... But it is otherwise with generosity. We never are generous except when in some respect we prefer some other person to ourselves, and sacrifice some great and important interest of our own to an equal interest of a friend or of a superior. [*ibid.*, 190-91]

Generosity therefore exhibits the self-sacrificing behavior characteristic of an altruistic act and Smith implicitly assumes that the abstract reasoning required to attain the perspective of the impartial spectator is potentially powerful enough to override feelings of narrow self-interest. In this respect, it is reason and imagination rather than emotion or feeling that is decisive in Smith's theory of altruistic charitable behavior. However, persons possessing the combination of "gentle" and "austere" virtues necessary for producing acts of generosity are relatively rare. In contrast, the desire for praise is a more universal motive to action in Smith and therefore a much larger supply of donors would exist if charitable acts brought favorable public attention. Smith allows for this self-regarding motive by arguing that the public naturally approves of actions which display "benevolent affections," a dimension which is relevant to the question, examined later, of whether or not private charity markets provide an efficient level of aid to the poor [*ibid.*, 39].

Another important dimension of Smith's theory of charity is that self-command may be required of the potential beneficiary as well as the benefactor if a charitable act is to be produced. Beneficiary self-command is pivotal because the benefactor, despite being "naturally sympathetic" to the distress of the former, nevertheless is a spectator whose emotions "will still be very apt to fall short of the violence of what is felt by the sufferer" [*ibid.*, 21]. Therefore, the potential beneficiary "can only hope to obtain [sympathy] by lowering his passion to that pitch, in which the spectators are capable of going along with him" [*ibid.*, 22]. Thus, self-restraint is the device by which the beneficiary's condition is revealed to the potential benefactor in a manner that will invite his/her fellow-feelings. Recalling that the humanitarian feelings of the benefactor (to become active) also generally requires a measure of self-restraint, it is clear that self-command is a kind of moral "investment" required of both parties in order to produce a harmony of sentiment leading up to an act of charity.⁵

The motive for investing in the virtue of self-command is described by Smith early in *TMS* in the section entitled "Of the Pleasure of Mutual Sympathy" [*ibid.*, 13-16]. Smith there observed that "nothing pleases us more than to observe in other men a fellow-feeling with all the emotions of our own breast" and he went on to add:

As the person who is principally interested in any event is pleased with our sympathy, and hurt by the want of it, so we, too, seem to be pleased when we are able to sympathize with him, and to be hurt when we are unable to do so. We run not only to congratulate the

successful, but to condole with the afflicted; and the pleasure which we find in the conversation of one whom in all the passions of his heart we can entirely sympathize with, seems to do more than compensate the painfulness of that sorrow with which the view of his situation affects us. [*ibid.*, 13; 15-16]

By arguing the potential mutual advantages of establishing sympathy, this passage would seem to provide a strong rationale for the natural development of private charity markets serviceable to the poor. However, as we shall see in the next section, Smith assumed a psychological disposition detrimental to the creation of such markets.

CHARITY AND THE POOR

Smith defined human sympathy broadly to refer not only to fellow-feeling for sorrow or pain that may be felt by the poor and unfortunate, but also to the joy and pleasure that the wealthy and fortunate are imagined to experience. In fact, Smith believed that "our propensity to sympathize with joy is much stronger than our propensity to sympathize with sorrow" despite the fact that "our sympathy with pain ... is generally a more lively and distinct perception than our sympathy with pleasure" [*ibid.*, 45, 44]. The reason that Smith provides for this behavior is a classic case of denial: humans have a natural aversion to painful experiences which causes them to suppress (deny) any emotional identification with those experiencing distress. Coupled with the tendency of the afflicted to conceal their condition out of shame, the result is a powerful set of psychological barriers discouraging acts of charity toward the poor:

It is agreeable to sympathize with joy... But it is painful to go along with grief, and we always enter into it with reluctance... The wretch whose misfortunes call upon our compassion feels with what reluctance we are likely to enter into his sorrow, and therefore proposes his grief to us with fear and hesitation: He even smothers the half of it, and is ashamed, upon account of this hard-heartedness of mankind, to give vent to the fulness of his affection. [*ibid.*, 45-46]

The result, according to Smith, is a natural disapprobation, even contempt, by society toward the poor.

In contrast, Smith argued that humans naturally respect and admire the rich because of the pleasure they tend to associate (however mistakenly) with wealth. Significant disparities in wealth first appeared during what Smith called the pasturage stage of society, a time in which charitable activity was directed toward the rich from the poor out of respect for their authority [Smith, 1978, 212].⁶ Later, during the agricultural (or feudal) stage of society, Smith again viewed charity as serving the interests of the wealthier governing classes. Consider, for example, Smith's discussion of "charity" in *The Wealth of Nations* as it emerged among the religious clergy and feudal landlords who controlled much of the wealth during the middle ages:

In the ancient state of Europe, before the establishment of arts and manufactures, the wealth of the clergy gave them the same sort of influence over the common people, which that of the great barons gave them over their respective vassals, tenants, and retainers... The tenants of the clergy were, like those of the great barons, almost all tenants at will, entirely dependent upon their immediate lords, and therefore liable to be called out at pleasure, in order to fight in any quarrel in which the clergy might think proper to engage them. Over and above the rents of those estates, the clergy possessed, in the tythes, a very large portion of the rents of all the other estates in every kingdom of Europe. The revenues ... exceeded greatly what the clergy could themselves consume; and there were neither arts nor manufactures for the produce of which they could exchange the surplus. The clergy could derive advantage from this immense surplus in no other way than by employing it, as the great barons employed the like surplus of their revenues, in the most profuse hospitality, and in the most extensive charity. Both the hospitality and the charity of the ancient clergy, accordingly, are said to have been very great. They not only maintained almost the whole poor of every kingdom, but many knights and gentlemen had frequently no other means of subsistence than by traveling about from monastery to monastery, under pretense of devotion, but in reality to enjoy the hospitality of the clergy. [(1776) 1976, 800-801]

Thus, Smith viewed most charity during the middle ages not as an altruistic gift but as a self-promoting economic exchange: by providing the means for economic subsistence to their tenants, the clergy and feudal lords extended their influence by receiving protective services and submission in return. From its inception in the pasturage stage of society to its later development in the feudal period, Smith therefore viewed "charitable" activity as consolidating the wealth and power of those in authority. In fact, in *TMS* Smith often lauds the act of military service which principally consists of sacrificing one's own interest to that of a superior and whose primary function is the preservation of the existing social order. Altruism and charity therefore play a prominent role in Smith's theory of social order, more so than as a transfer mechanism for attaining any sort of distributive justice norm [Smith, (1759) 1976, 226].

In contrast to military service, Smith is comparatively silent in his call for altruistic acts of charity for the poor despite a genuine concern for the poor and persistent poverty (and charitable activity) during his day.⁷ Although one can make a compelling case that Smith saw the problems confronting the poor as being self-correcting under an economic system of competitive markets, his comparative neglect of alternative methods of aiding the poor is nevertheless unfortunate since Smith himself hardly believed that the system of natural liberty which he was recommending would ever exist. Given this reality, all that remains are the psychological barriers prevent-

ing private voluntary aid to the poor discussed earlier, resulting in the economic and psychological alienation of the poor from the wealthier classes. It is interesting, therefore, to investigate the case for government intervention on behalf of the poor within the context of Smith's own psychological thought assuming the absence of a fully functioning competitive economy, or at least one that was not as beneficent to the poor as Smith might have imagined.

In *The Theory of Moral Sentiments*, Smith was very cautious about giving the government direct authority to require acts of beneficence, but he did not entirely rule out this function, stating that "[t]he civil magistrate... may prescribe rules ... which not only prohibit mutual injuries among fellow-citizens, but command mutual good offices to a certain degree" [(1759) 1976, 81].⁸ However, government enforcement of beneficence was a matter of "the greatest delicacy" and Smith expressed concern that "to push it too far is destructive of all liberty, security and justice" [*ibid.*, 81]. It is interesting, however, that Smith's own social and psychological thought provides at least a provisional theoretical justification for a government role promoting beneficent acts such as charitable assistance to the poor. First, there is the transaction cost problem inherent to private charity markets due to the tendency of the poor to conceal their condition from their potential benefactors.⁹ Second, a failure to establish sympathy between rich and poor (which prevents voluntary private charitable donations to the poor) constitutes a loss to society since Smith is explicit that third party spectators benefit from observing benevolent actions:

Generosity, humanity, kindness, compassion, mutual friendship and esteem, all the social and benevolent affections, when expressed in the countenance or behavior, even towards those who are not particularly connected with ourselves, please the indifferent spectator upon almost every occasion... We have always... the strongest disposition to sympathize with the benevolent affections. They appear in every respect agreeable to us. We enter into the satisfaction both of the person who feels them, and of the person who is the object of them. [*ibid.*, 38-9]

The fact that third party spectators naturally tend to approve of both the charitable actions of the benefactor and the gratitude of the beneficiary, creates what Smith calls a "double sympathy", and although the positive externalities that Smith is describing arise from the simple expression and exchange of friendly emotions, it is logical (indeed implicit in the meaning Smith assigned to "generosity") that a charitable transfer of more conventional goods or services from rich to poor is capable of generating the same effect [*ibid.*, 40]. The existence of positive externalities suggests the possibility that a free market society may lead to too little expression of benevolent feelings (and the completion of too few charitable acts) from a social utility-maximization perspective and, in line with the classic economic remedy for a public goods problem, government should encourage the production and exchange of amicable emotions and charitable services to correct for this potential market failure.¹⁰

This argument for government intervention on behalf of the poor, however, needs to be qualified if the donor derives a personal benefit from the externality created by his or her charitable act. According to Smith, individuals are most powerfully driven by a desire for social approbation and not wealth *per se*. Elsewhere Smith asserts that "[n]o benevolent man ever lost altogether the fruits of his benevolence. If he does not always gather them from the persons from whom he ought to have gathered them, he seldom fails to gather them, and with a tenfold increase, from other people" [*ibid.*, 50-1, 255]. Therefore, to the extent that charitable giving is an effective way for individuals to gain favorable public attention, private charitable activity may actually lead to overprovision of aid as when, for example, donations are used to signal social or economic status [Glazer and Konrad, 1996]. On the other hand, if we take a typical social problem associated with poverty during Smith's day—that of undesired vagrants whose roamings contributed to the spread of disease [Marshall, 1926, 225-45]—it is also certainly possible that donors making private contributions to mitigate vagrancy may not capture all of the positive externalities that they create. Aside from the spillover benefits to those approving of a charitable act, there may be additional positive externalities not fully appropriated by the donor such as protecting other members of society from the pain of observing unsightly poverty or reducing health risks to society at large. The general point that private charity may either under- or over-provide aid to the poor, implicit in Smith's writings, was later made explicit by John Stuart Mill who argued that the uneven and irregular distribution of private charity provides a case for at least a minimal level of government support on behalf of the poor [Mill, 1883, 589-92].

The case for government intervention to correct for private charity market failure also needs to be assessed in light of Smith's moral philosophy, in particular his ideas on propriety and merit. The propriety of a charitable act (whether public or private) depends on the legitimacy of "the cause or object which excites it" and its merit according to whether the effect it produces is "beneficial or hurtful" [(1759) 1976, 67]. For example, a sense of propriety depends on donor identification with the cause of the recipient's distress. In practice, information about the circumstances surrounding a recipient's misfortune may be difficult to obtain and compounds the transaction cost problem due to segregation of rich and poor identified earlier. Sensitive to the frequent difficulty of obtaining the requisite information to establish actual sympathy, Smith introduced the idea of "conditional sympathy" [*ibid.*, 18] utilized under conditions where it is infeasible (or costly) to know (or inform ourselves about) all the circumstances surrounding another's misfortune. Conditional sympathy provides a basis for developing a set of "general rules derived from our preceding experience" which helps correct for any impropriety in our conduct due to our not having full knowledge of relevant circumstances necessary to establish actual sympathy [*ibid.*, 18]. On the one hand, information barriers preventing full sympathy between donor and recipient suggest the futility of designing any government welfare policy completely adapted to the wants of donor and recipient. On the other hand, the necessity of employing general rules to govern moral conduct in a world of imperfect information might be reasonably interpreted as providing a second best justification for gov-

ernment intervention to articulate and implement those "general rules" of moral conduct.

Finally, in order to fully approve of a charitable act, donors also must be sympathetic to the merit or consequences of providing relief. On grounds of merit, Smith was very suspicious of both private and public charity as practiced during his lifetime. As is well known, Smith was strongly opposed to the settlement requirements in England's poor laws on the grounds that it hindered the mobility of poor laborers and contributed to their economic destitution [Smith, (1776) 1976, 152-57]. In addition, Smith believed that the "many pensions, scholarships, exhibitions, bursaries, etc." from public and private sources designed to educate people for the clergy was having the unintended consequence of artificially increasing labor supply and depressing wages to subsistence levels in related occupations [*ibid.*, 146].¹¹ Smith was also well aware of a potential "moral hazard" problem accompanying charitable assistance of this sort, noting that private educational endowments "have necessarily diminished the necessity of application in teachers" [*ibid.*, 760]. These examples of demerit associated with charitable activity do not, of course, imply that Smith was dogmatically opposed to all forms of public or private charity, but it does make clear that Smith was not content to evaluate government welfare policy or private charity exclusively in terms of intent or motive. Instead, social utility, propriety and merit were all relevant moral dimensions in need of consideration.

CHARITY IN A COMMERCIAL SOCIETY

The period from 1660 to 1780 in England has been called the "Age of Benevolence" and, indeed, a fairly extensive system of public and private charity existed during Adam Smith's lifetime which coincided with the emergence of a commercial society [Owen, 1964, 11-88]. In terms of private charity, one of the key developments in this period was the emergence of private charity schools and hospitals which were voluntary associations whose financing and operations mostly depended upon the small contributions of large numbers of individual subscribers rather than a single large contribution of a generous founder [Owen, 1964, 11-13]. Although Smith does discuss the private versus public education question in Book V of *The Wealth of Nations*, he does not mention the private charity hospital system or other eleemosynary institutions, which is unfortunate since it leaves an incomplete picture of Smith's views on public versus private philanthropy in the various areas of assistance affecting the poor during his day. Instead, *WN* remains largely a theoretical work dedicated to arguing the economic benefits of competitive markets for all classes of society including the poor. In this context, it is important to ask whether the commercial society envisioned by Smith, if fully operative and evaluated from Smith's own ethical perspective, might overcome or render irrelevant the factors tending to prevent the development of efficient private charity markets identified in the previous section.

Clearly, one of the central arguments of *WN* is that the long run demand for charity is substantially reduced under a system of competitive markets due to "that

universal opulence which extends itself to the lowest ranks of the people" [Smith, (1776) 1976, 22]. That is, the need for acts of economic altruism becomes less urgent with the spread of free markets because the demand for labor and the wages of workers rise most rapidly under these conditions. This decrease in the demand for charity is fortuitous because Smith's analysis in *WN* suggests that the supply of charity also tends to decrease under competitive capitalism despite growing national wealth. First, within the emerging capitalist class of merchants, manufacturers and farmers, competition tends to decrease individual rates of profit in the long run, implying that charitable acts of individual capitalists endangers their own economic position and conflicts with prudential considerations (unless accompanied by social approval). Smith also added a section entitled "Of the corruption of our moral sentiments, which is occasioned by this disposition to admire the rich and the great, and to despise or neglect persons of poor and mean condition" to the final edition of *TMS* which suggests that Smith was increasingly concerned about excessive ambition for status and wealth undermining a sense of civic duty among middle class capitalists in manufacturing, commerce and agriculture [Dwyer, 1987, 169-73]. In principle, the decrease in the supply of charity from these influences is offset by the prudential savings of capitalists which increases the demand for labor and raise the wages earned by the working poor. This is, of course, Smith's famous economic invisible hand which, in the moral realm, substitutes prudence for beneficence as the mechanism providing economic assistance to the poor.

Second, Smith believed that as the economic status of the working class improved in the commercial society there was an accompanying moral decay due to overspecialization which undermined the supply of charity from this segment of society:

The man whose whole life is spent in performing a few simple operations, of which the effects too are, perhaps, always the same, or very nearly the same, has no occasion to exert his understanding, or to exercise his invention in finding out expedients for removing difficulties which never occur. ... The torpor of his mind renders him, not only incapable of relishing or bearing a part in any rational conversation, but of conceiving any generous, noble, or tender sentiment, and consequently of forming any just judgment concerning many even of the ordinary duties of private life... [(1759) 1976, 781-2]

Smith is asserting that in an advancing commercial society there is a narrowing of human experience among the working class which dulls both individual initiative and a sense of public duty. Recalling that an altruistic act requires "sympathy" with another person's situation obtained through imagination, breadth of understanding and reason, the fact that workers are not developing these faculties in their everyday lives points to a serious barrier restricting the supply of charity from this source quite aside from obvious income constraints.

Finally, a traditional source of wealth and paternalistic support for the poor in England (and Europe generally) had been the landed nobility. Although Smith be-

lieved that wealth tended to promote humanistic feelings, especially toward those in physical proximity, the emergence of a commercial society implied a disruption of feudal ties and separated the upper gentry from their traditional dependents. Moreover, while Smith referred to "the generosity which is natural to their [e.g., landlords] station," elsewhere he faulted their lack of self-command partly attributed to the fact that their wealth was principally derived from unearned rental income [(1776) 1976, 462; 265]. The landlord class, therefore, was susceptible to that "indolent benevolence" spoken of in *TMS* and was an unreliable supplier of charity during the commercial stage of society, particularly given the temptations of emerging new consumer products.

In sum, in *WN* Smith provided a theory of charity in which the supply and demand for charity would naturally decline during the expansion of a free market commercial society. However, it needs to be emphasized that this adjustment was only a long run tendency in a first-best world of competitive markets. As Smith was well aware, the commercial society about which he wrote was never fully competitive: laws of corporation and apprenticeship originating in medieval towns prevented the mobility of capital and labor, at the same time permitting early capitalist development. This is the context for Smith's analysis of the early stages of commercial growth during which time the Catholic clergy (and feudal lords) began expending their substantial wealth on new products made available by capitalists rather than on charity:

The gradual improvement of arts, manufactures, and commerce, the same causes which destroyed the power of the great barons, destroyed in the same manner, through the greater part of Europe, the whole temporal power of the clergy. In the produce of arts, manufactures, and commerce, the clergy, like the great barons, found something for which they could exchange their rude produce, and thereby discovered the means of spending their whole revenues upon their own persons, without giving any considerable share of them to other people. Their charity became gradually less extensive, their hospitality less liberal or less profuse. Their retainers... were provoked and disgusted by the vanity, luxury, and expense of the richer clergy, who appeared to spend upon their own pleasures what had always before been regarded as the patrimony of the poor. [*ibid.*, 803-4]

The growth of commerce was therefore initially inimicable to the system of "charity" (keeping in mind its self-interested roots) which had traditionally provided economic support to the poor during the middle ages. Absent laws restricting the mobility of capital and labor, Smith's economic analysis in *WN* suggests that commerce would have improved the lot of the poor by increasing the demand for labor, but the short-run problem was that the consumption opportunities which capitalists provided for the clergy and landed nobility were diverting resources away from an established system of paternalistic charity upon which the poor had come to depend. Instead of removing the barriers preventing the mobility of labor and capital (Smith's policy

prescription), the English government responded by enacting a series of poor laws marred by settlement requirements which merely compounded the problems of the poor according to Smith. More broadly, Smith argued that mercantilist policies not only impeded the mobility of resources, but also prematurely distorted investment away from the agricultural sector and diverted domestic agricultural and manufacturing produce abroad, all of which left the poor vulnerable in the accelerated transition from an agricultural to a commercial society.

Accompanying the economic misallocations of mercantilism was an equally significant moral maladjustment. Never one to applaud the morality of capitalist merchants or manufacturers, Smith was concerned that their class interest was perpetuating a system of protectionism that had begun to infect "country gentlemen and farmers" [*ibid.*, 462]. Beyond the direct economic harm these protectionist measures inflicted on the poor, Smith's analysis points toward a complementary moral concern, namely that an emerging class of capitalists not subject to the disciplining effect of competition and accustomed to the protection afforded by government policies, would fail to learn the lessons of self-command necessary for the development of a sense of public duty and a capacity for altruistic behavior. The danger to the poor was that this new privileged class of capitalists would be replacing a wealthy class of landed nobility but without their adherence to a paternalistic tradition. Indeed, the landed nobility was increasingly alienated from the poor as they turned more of their income toward consumption and commercial ventures outside of agriculture.¹² As the landed nobility partly divested themselves of their agricultural interests, Smith believed that agricultural productivity would increase under a new class of industrious farmers, but this process was slowed by the law of entails and, as mentioned previously, he also implicitly feared that this new middle-class gentry was susceptible to the moral corruption associated with emulating capitalist merchants and manufacturers.¹³ Meanwhile, although there is evidence of improved conditions for many in the lower classes during this historic transition from an agricultural to a commercial society [Smout, 1969, 302-331; 1983, 45-72], poverty continued to plague many, including landless farm dependents turned wage-earners and others disenfranchised by the long process of land enclosure but not fully assimilated into the commercial and manufacturing sectors of the economy.

CONCLUSION

In *An Inquiry into the Nature and Causes of the Wealth of Nations*, Adam Smith presented a first-best theory in which the need for charity diminishes in the long run as the condition of the poor improves under the prudent and just behavior of capitalists in a competitive free-market economy. However, the vision of capitalist society that emerges in Smith's thought in the absence of a fully functioning competitive market economy is a much more distressing one from the standpoint of the poor. Removed from the economic mainstream, the poor have a natural tendency to conceal their misfortune out of shame, and the wealthy (as well as its middle class aspirants) have an inclination to distance themselves from the poor out of contempt. Un-

der these conditions, private charity markets are inefficient providers of aid to the poor and their potential benefactors.¹⁴ Furthermore, the supply of altruistically motivated benefactors is unlikely to increase, and may very well decrease, in the transition from feudalism to capitalism according to Smith's theory. The stagnant or declining supply of donors under capitalism is not due to a romantic conception of chivalrous behavior during feudal times—on the contrary, Smith viewed most charity during the middle ages as being self-interested—rather, it is due to the difficulty of developing the rare combination of virtues (beneficence coupled with self-command) required for acts of generosity within either social setting. A qualification to the argument that private charity markets tend to underprovide aid to the poor stems from the fact that Smith allowed for the possibility that benefactors might appropriate public approval from their charitable acts—a powerful motive to action in Smith's theory of human behavior. However, it is not clear that donations to the poor would be the most attractive form of charity for achieving this type of social recognition nor would the nature and level of charity necessarily be efficiently distributed among the poor population even if this motive was fully operative.

Given the potential failure of private charity markets to efficiently provide aid to the poor, a modern welfare-theoretic case for government intervention on behalf of the poor can be constructed from Smith's writings. However, the problem of determining the optimal institutional mix for addressing the problem of the poverty is inherently a second-best one due to inefficiencies associated with both private and public sector responses [Weisbrod, 1988, 5-7]. Also, the moral dimension to Smith's theory of charity must be taken into account. Smith viewed altruistic charity as being a consequence of a moral judgment on the part of the donor, a judgment influenced by considerations of propriety and merit which both depend, in part, on recipient behavior. For example, a uniform means-tested government welfare policy might be viewed by some donor-taxpayers, if not Smith himself, as conflicting with both propriety (e.g., by failing to distinguish between "deserving" and "undeserving" poor) and merit (e.g., by damaging work incentives and inviting welfare dependency). On the other hand, establishing a government welfare policy flexible enough to be consistent with local considerations of propriety and merit may require a degree of decentralization which itself can lead to eligibility criteria (e.g., settlement requirements) damaging to the poor, as Smith was well aware. In fact, our analysis of Smith's thought points to a more fundamental dilemma associated with redistributive welfare policy. If market distortions created by government regulation of the economy necessitate a reliance on voluntary charitable acts to aid the poor, then another type of market failure surfaces: the potential inefficiency of private charity markets in providing aid to the deserving poor. On the other hand, if in the name of private charity market failure, charity is tied to general rules of "beneficence" or "distributive justice" for which there is a government duty to enforce, then a corresponding conjuncture of recipient "rights" or "entitlements" is established which may undermine habits of prudence (diligence and commitment to work) and even beneficence (gratitude toward taxpayer-donors for aid) within the recipient population. Furthermore, if charity becomes a public obligation delivered through the more impersonal channels of government, then charity runs the risk of losing the element of voluntary personal choice fundamental to Smith's

theory of moral behavior. These are prominent issues in the current debate about the nature and scope of the modern welfare state and it is a tribute to Adam Smith that he continues to provide a fertile economic and moral framework for addressing this important public policy issue.

NOTES

1. In the final edition of *TMS*, Smith added a Part VI which outlines his ethical system consisting of four types of virtue: prudence, justice, beneficence and self-command. The economic functions of prudence, justice and self-command have been previously examined by researchers stressing the connections between *The Wealth of Nations* and *TMS* [Macfie, 1967; Rosenberg, 1990], as well as by those emphasizing the differences between Smith's ethological and economic analyses [Brown, 1994]. For a rare economic analysis of Smith's virtue of beneficence, see Campbell [1967].
2. Smith's public education proposal was also partly motivated by the public good Smith assigned to tempering religious enthusiasm and superstition among the lower class and a concern for their moral as well as material well being.
3. See Khalil [1990] for a recent discussion of a sense of duty as a factor governing human behavior in Smith's writings in contrast to the standard utility-maximization calculus assumed by modern economic theory.
4. Similarly, Rawls derives disinterested justice principles from his "veil of ignorance" construct [Rawls, 1971, 136-42].
5. Note, however, that the self-command required of the recipient is not exactly the same as that required of the donor. The self-command required of the recipient is governed by public (i.e., potential donors') opinion whereas the self-command of the donor arises from an inner sense of duty instructed by the perspective of an imaginary impartial spectator.
6. In his listing of the natural order of those persons "recommended to our beneficence," Smith gave equal footing to "the rich and the powerful" and "the poor and the wretched," both of whom were ranked behind those in close "connection with ourselves" (e.g., family and friends), those with admirable "personal qualities" and those owed a debt of gratitude for "past services" [*TMS*, 225]. Admiration for the rich was also the reason why Smith believed that people were inclined to be more charitable toward wealthier persons recently fallen into poverty than those perpetually in a state of hardship [*TMS*, 144].
7. On Smith's unusual degree of concern for the poor, see Himmelfarb [1982, 46-62]. During Smith's day, Great Britain had a mixed agricultural and industrial economy [Hollander, 1973, 112] with poor in both rural and urban sectors partly due to periodic unemployment associated with the transition from an agricultural to a manufacturing economy (see Lenman [1981, 19-20; 118-119] on poverty in eighteenth century Scotland and Langford [1989, 150-55] on poverty in eighteenth century England). For the origins of this transition from agriculture to manufacturing in Great Britain and the evolution of public and private charity to combat poverty during this period, see Appleby [1980, 129-53], Himmelfarb [1983, 25-36], Langford [1989, 128-45; 481-87], Marshall [1926] and Owen [1964].
8. See Young and Gordon [1996, 17-19] on Smith's support for government policies aimed at distributive justice.
9. It might be objected that if demanders of charity (e.g., the poor) do not reveal their true distress to the potential suppliers of charity (e.g., the rich), then this is simply a matter of consumer "preference" and not a transaction cost problem. However, the poor's "preference" to conceal their condition is partly an *endogenously* determined behavior which stems from the shame they experience by knowing that others disapprove of their condition. Thus, there is a true transaction cost problem in that potential suppliers of charity (the rich with the requisite benevolence and self-command) do not know what demanders of charity (the poor) really need or want.
10. This is a somewhat modified version of the interdependent utility argument for government intervention suggested by Baum [1992, 149-50].
11. Smith argued that *in practice* our sense of merit depends on the *actual* consequences of an action even if remote or unintended [*TMS*, 93].

12. Langford states that "it is not too much to speak of a crisis of paternalism in the 1760s and 1770s" and speaks of "an immense gulf between upper and lower classes in the countryside, bridged only by still more snobbish gentlemen farmers and cynical, monopolistic merchants" [Langford, 1989, 441, 442].
13. On the evolution of farmers from tenants at will to freeholders and on entails as a hindrance to agricultural improvement see Smith [WN, 384-95].
14. Hansmann [1986] has argued the advantages of nonprofit versus for-profit charitable organizations when information about quality or quantity of service is difficult for donors to monitor, but whether the private nonprofit is more efficient than the public sector in delivering charitable services when information is imperfect is as yet unsettled in the literature [James and Rose-Ackerman, 1986, 69-77] and the psychological source of the information problem and market failure identified by Smith has not been addressed.

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