

Adam Smith's "Two Distinct Benefits" from Trade: The Dead End of "Vent-for-Surplus" Interpretations

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In the last few decades, Adam Smith's theory of international trade has seen a revival, after having been neglected for a long time. This renaissance can arguably be attributed to Hla Myint (1958), who highlights the advantages of a Smithian trade theory compared to the static theory of comparative advantage. Myint distinguishes between two different gains from foreign trade in Smith's theory, a vent-for-surplus and a productivity gain. From those benefits, he derives two separate theories of international trade, namely, a vent-for-surplus theory and a productivity theory, which he ascribes to Smith. This categorization has been successful if measured by its adoption by other scholars. However, there have been arguments about the interrelation of both theories, whether they are inseparable, distinct, or mutually exclusive. Additionally, the vent-for-surplus gain has caused some debates about its possible interpretation and Smith's original application.

In this article, I do not want to add to either of these two discussions. Rather, I will disprove Myint's widely adopted categorization. This categorization cannot be sustained when compared to what Smith actually writes. It is rather based on a misreading of one paragraph of *The Wealth*

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of Nations (WN). For Smith, imports and exports constitute the “two distinct benefits” from foreign trade, which he expounds in *The Wealth of Nations*. Smith does not distinguish between a vent-for-surplus gain and a productivity gain from foreign trade and he has no vent-for-surplus theory in a modern sense.

The article is organized as follows. I will first show how Myint comes to the conclusion that Smith’s theory of international trade contains a vent-for-surplus and a productivity theory and how this separation has been discussed in the literature. Afterward I will compare this categorization to *The Wealth of Nations*. I will discuss the meaning of the terms “surplus produce” and “superfluities” in both *The Wealth of Nations* and the contemporary literature. I will show why imports and exports are both beneficial according to Smith. Moreover, the reasons why Myint and others have misinterpreted Smith’s gains from trade will be discussed. Afterward, I will examine why other classical economists, above all David Ricardo and John Stuart Mill, criticized Smith. Their criticism is not directed against a modern vent-for-surplus argument and has been misunderstood as well. The article ends with a short conclusion.

1. Smith’s Two Alleged Theories of International Trade

In an influential article, Hla Myint (1958) argues that Adam Smith uses two separate gains to show that foreign trade is beneficial for a nation. Myint draws on the following paragraph of *The Wealth of Nations*:

Between whatever places foreign trade is carried on, they all of them derive two distinct benefits from it. It carries out that surplus part of the produce of their land and labour for which there is no demand among them, and brings back in return for it something else for which there is a demand. It gives a value to their superfluities, by exchanging them for something else, which may satisfy a part of their wants, and increase their enjoyments. By means of it, the narrowness of the home market does not hinder the division of labour in any particular branch of art or manufacture from being carried to the highest perfection. By opening a more extensive market for whatever part of the produce of their labour may exceed the home consumption, it encourages them to improve its productive powers, and to augment its annual produce to the utmost, and thereby to increase the real revenue and wealth of the society. (WN IV.i.31)

Myint argues that Smith’s “two distinct benefits” are first a vent-for-surplus gain, because international trade “gives a value to their superfluities,” and second a productivity gain, because international trade enhances the division of labor and improves “its productive powers.” From the first gain, Myint (1958, 318) derives the “‘vent for surplus’ theory of international trade,” which assumes that an international market “provides an outlet for the surplus product above domestic requirements.” From the second gain, Myint derives the “productivity theory,” which shows how “international trade also improves the division of labour and raises the general level of productivity within the country” (318).

The classification of the gains from foreign trade in Smith’s theory into a vent-for-surplus gain and a productivity gain has been widely adopted since Myint first proposed it in 1958.¹ Equally, the differentiation between a vent-for-surplus theory and a productivity theory in Smith’s theory of foreign trade was not questioned much. However, most scholars emphasize the productivity theory, according to which foreign trade extends the market and enables an enhanced division of labor and productivity growth. This productivity theory has built Smith’s reputation in international economics, after he was generally seen as a poor trade theorist because he failed to discover the theory of comparative advantage.² This reappraisal was supported by New Trade Theorists, who claim Smith as one of their predecessors, especially regarding increasing returns (see, e.g., Krugman 1990, 4).³

1. Myint (1958, 318n) refers to John Stuart Mill and the international trade expert John H. Williams for the term “vent-for-surplus.” Mill ([1848] 1965, 591) uses the phrase “a vent for its surplus” in connection with Smith, and Williams (1929, 203) writes about “Mill’s famous objection to Adam Smith’s ‘vent for surplus’ principle.” However, they do not divide Smith’s trade theory into a vent-for-surplus and a productivity approach. Myint introduced this distinction first, as he himself acknowledges (Myint 1977, 242). The term “vent-for-surplus” itself was not new but used widely, as the following examples demonstrate. James Syme (1821, 291) notes that external trade is beneficial “by furnishing a vent for the surplus produce” (see also 327). James Mill ([1807] 2006, 138) argues against the idea that foreign trade “furnish[es] a vent for the produce of the industry of the country,” and Thomas Mun ([1621] 1969, 50) writes that England “must finde meanes, by Trade to vent our superfluities.” Even David Ricardo ([1822] 2004, 241) writes that “under a system of free trade . . . if an abundant harvest occurred . . . after an inconsiderable fall of price, a vent for the superfluous produce would be immediately found in exportation.”

2. Smith’s theory of international trade has been depicted by international trade economists as a theory of absolute advantage and thus as a simple case of the more sophisticated theory of comparative advantage. However, this representation, which is included in most modern textbooks on international economics, is an adulteration of Smith’s writings (Schumacher 2012).

3. Smith’s concept of the division of labor is often equated with increasing returns. The neoclassical concept of increasing returns implies that when all factor inputs are increased by an identical proportion, output increases in a greater proportion. Smith’s concept of the division of labor, by contrast, is not so narrow but much more sophisticated.

The vent-for-surplus theory, in contrast, has been more controversial. Smith uses the terms “surplus produce” and “superfluities” in connection with foreign trade in several paragraphs of *The Wealth of Nations*. In one often quoted paragraph, Smith states, “When the produce of any particular branch of industry exceeds what the demand of the country requires, the surplus must be sent abroad, and exchanged for something for which there is a demand at home. Without such exportation, a part of the productive labour of the country must cease, and the value of its annual produce diminish” (WN II.v.33). In another paragraph Smith writes that “in every period, indeed, of every society, the surplus part both of the rude and manufactured produce, or that for which there is no demand at home, must be sent abroad in order to be exchanged for something for which there is some demand at home” (WN III.i.7).⁴

The scope of its application and what Smith meant by it has led to discussion among scholars. The different interpretations can be divided into four groups, which are not necessarily mutually exclusive. First, it is claimed that the vent-for-surplus theory can be applied only to certain nations or goods. In his original approach, Myint (1958) argues that Smith applies the vent-for-surplus theory only to underdeveloped nations. This is repeated by others (Gomes 1987, 2003; Kindleberger 1964; Winch 1965), while Denis O’Brien (1983, 93) suggests that it applies merely to advanced nations. Myint later extended the vent-for-surplus theory to developed countries but still excluded, in alleged accordance with Smith, “highly advanced ‘commercial nations’” (1977, 243). Some stress that Smith’s vent-for-surplus gains can be realized only with agricultural or primary goods (Myint 1977; Ros 2000) or in case of joint products (Kurz 1990, 1992; West 1994).

Second, it is argued that Smith’s vent-for-surplus theory is bound to certain presumptions or requirements, such as underemployed resources (Bloomfield 1981; Findlay and Lundahl 1994; Kibritçioğlu 2002; Magnusson 2004; Meier 1994; Myint 1977, 1958; O’Brien 1975; Platteau 1978; Rima 2004; Ros 2000; Staley 1973; Winch 1965), inelastic domestic demand (Hollander 1973; Myint 1958; O’Brien 1975; Platteau 1978; Staley 1973), internal immobility or fixed resources (Myint 1958; Staley 1973), specificity of resources or factors (Hollander 1973; Myint 1958; Platteau 1978), indivisibilities (Winch 1965), a highly skewed resource base

4. Other paragraphs referred to in relation to Smith’s vent-for-surplus theory are WN I.xi.c.4, II.v.4–6, II.v.16–18, II.v.24, II.v.34, II.v.36, III.i.1–2, III.iii.20, III.iv.5, IV.iii.c.4, IV.vii.c.4–9, IV.vii.c.22, and IV.vii.c.47–50.

(Kindleberger 1964), overproduction in general (Kindleberger 1964; Morales Meoqui 2010; Rutherford 2002; Negishi 2004; West 1994), and poor internal communications (Winch 1965, 8).

Third, some authors do not only stress the difference between the vent-for-surplus and the productivity theory but also assert that the former is incompatible with Smith’s system of natural liberty and therefore at variance with Smith’s overall theory. These authors often refer to David Ricardo and John Stuart Mill, who allegedly brought forward a similar argument. To this group belong Leonard Gomes (1987), Charles E. Staley (1973), and Jorge Morales Meoqui, who refers to Smith’s vent-for-surplus gain as “error,” “theoretical flaw,” and “fallacy” (Morales Meoqui 2010, 42, 45). Added to this group can be those who agree that there is an incompatibility between both, but that it can be solved. Lars Magnusson argues that the productivity theory is Smith’s “general principle,” but that it applies only in the long run. He implies that Smith “must . . . have been sceptical as to whether this principle provided a very realistic picture of the present,” because “there was a limit to the dynamics of market forces” (Magnusson 2004, 34). Magnusson concludes that the vent-for-surplus theory holds in the short and medium terms. Nerio Naldi (1996, 212) claims that Smith’s references to surplus and superfluities indeed “conflict with some fundamental propositions of the WN.” However, this should be seen as a “rhetorical form of speech” and should not be taken at face value.⁵

Fourth, some have questioned that both gains lead to two different theories of international trade. Gottfried Haberler (1959, 9n) argues that Myint’s distinction is “unconvincing” and suggests that the vent-for-surplus situation is “simply an extreme case of differences in comparative cost.” Other authors emphasize that the “surplus” is mainly the result of increasing returns and thus of specialization, as does Takashi Negishi (1985, 1989). More recently, Negishi (2004, 34, 37) has similarly argued that the productivity theory and the vent-for-surplus theory should be understood “as two parts of Smith’s single disequilibrium theory of inter-

5. Naldi refers to Smith’s *Lectures on Rhetoric and Belles Lettres* (LRBL) and uses Smith’s distinction between didactical and rhetorical discourse, the former being characterized by putting “before us the arguments on both sides of the question in their true light,” while the latter “endeavours by all means to persuade us; and for this purpose it magnifies all the arguments on the one side and diminishes or conceals those that might be brought on the side contrary to that which it is designed what we should favour” (LRBL i.149–50). Naldi argues that Smith uses the rhetorical method when writing of “surplus” and “superfluities.”

national trade.” They both are “an indispensable part of Smith’s disequilibrium (or path-dependence) theory of international trade,” with the vent-for-surplus theory being “clearly a disequilibrium theory which explains the cause of international trade in excess supply.” Both gains are seen as inseparable. They do not occur independently but are complementary. Robert Blecker (1997, 530) argues that “Smith’s apparently separate concepts of trade can thus be unified as a theory of an *international division of labour*.” Andrea Maneschi (1998, 48) describes the productivity and the vent-for-surplus theory “as two sides of a coin,” and Bruce Elmslie and Norman Sedgley (2002, 714) state that the “two gains from trade described by Smith are codependent” (see also Elmslie and Sedgley 2003).

Yet each of these four groups exposes some inconsistencies. First, Smith does not limit the terms “surplus produce” and “superfluities” to certain nations or certain goods. Rather, he talks of “every period, indeed, of every society” and refers to diverse goods as surplus produce.⁶ Second, although the listed assumptions are all conceivable explanations of a vent-for-surplus theory, they are not made by Smith himself, even though some authors might claim this. The third group raises the question why Smith would not have noticed such an incompatibility himself. Since he often refers to “surplus produce” and “superfluities” in connection with foreign trade, it is unlikely that Smith just overlooked such a mistake. Magnusson’s explanation of short- and long-term developments is in itself consistent but not given by Smith himself.⁷ Naldi’s interpretation that Smith uses a rhetorical discourse when he uses the terms “surplus produce” and “superfluities” is superfluous if my interpretation below is correct. There is no need to explain these terms as a rhetorical device, which leads to the question whether the whole *Wealth of Nations* is merely a rhetorical discourse. Smith uses those terms not only when he polemicizes against mercantilist policies but throughout *The Wealth of Nations*.⁸ The fourth group

6. An extensive criticism of Heinz Kurz’s (1990, 1992) joint products interpretation can be found in Elmslie 1996.

7. Magnusson is probably aware of this deficiency of his argument, which is why he adds that this is an alternative interpretation “which might be even more realistic, given what we know of Smith” (2004, 34).

8. Smith does not explicitly refer to the distinction between rhetorical and didactical discourse in *The Wealth of Nations*. However, *The Wealth of Nations* was intended as a scientific work and not merely as a polemic work against prevailing policies. Smith refers to the didactical discourse as “the best in all matters of Science” (*LRBL* ii.135), and it is thus implausible that he used the rhetorical method throughout *The Wealth of Nations*. It could be argued that he uses this method in book IV, but it is harder to claim that books I–III are rhetorical rather than didactical according to Smith’s definitions of those methods, as Naldi implies (see also Brown 1994, 9–22, 162–64).

raises the question why, if both gains were inseparable, would Smith talk of these as “two distinct benefits” from foreign trade?

There is, however, one point of agreement between all authors in these four groups. They do not question Myint’s categorizations per se. Authors in the first three groups assume that Smith uses the vent-for-surplus gain and the productivity gain as two separate approaches in his theory. Authors in the last group do not accept Myint’s conclusion that both gains lead to separate approaches. They stress that both gains are complementary and are even interdependent. These authors have thus pointed to the right direction, and I will use some similar arguments for my own interpretation below.⁹ Yet they do not repudiate Myint’s categorization outright. They still uphold that Smith himself classified the gains from trade accordingly.

2. Smith’s “Two Distinct Benefits”

In this section I will show that Myint’s categorization, although it has been influential, is wrong. On that point, I will first discuss the meaning of the terms “surplus produce” and “superfluities” in Smith’s writings and in the contemporary literature. Afterward, I will show whereof Smith’s “two distinct benefits” from foreign trade are comprised. Reasons why Myint and others misinterpreted Smith are given subsequently. Additionally, the criticism of Smith’s gains from foreign trade by nineteenth-century classical economists will be outlined, since it too has been misunderstood in the context of the debate about Smith’s alleged vent-for-surplus theory.

The Terms “Surplus Produce” and “Superfluities”

Smith does not use the phrase “vent-for-surplus,” but he often speaks of “surplus produce” and “superfluities.” The division of labor, with which *The Wealth of Nations* begins, leads to a specialization of laborers. As a result, they do not produce merely for their own consumption, but they need to exchange some part of their produce for other products that they are in need of. This part of the produce is termed by Smith “surplus produce”: “The certainty of being able to exchange all that surplus part of the produce of his own labour, which is over and above his own consumption, for such parts of the produce of other men’s labour as he may have

9. In a previous article, I myself supported this position in a short remark (Schumacher 2012, 59–60).

occasion for, encourages every man to apply himself to a particular occupation" (WN I.ii.3).¹⁰ All goods that are produced not for the consumption of their respective producer but for the market are described as surplus produce. As we will see in the next paragraph, such surpluses exist because there is a market for them. They would not be produced without a market. An effective demand is the precondition for the production of a surplus.

In this way, Smith describes the division of labor in different human societies as an exchange of surplus produce, starting with "a tribe of hunters or shepherds" (WN I.ii.3). In a "civilized society," the "exchange of rude for manufactured produce" between towns and countryside is described as an exchange of surpluses: "The town affords a market for the surplus produce of the country" (WN III.i.1). The same is true for colonial trade (WN IV.vii.c) and for foreign trade. If the market is extended beyond national borders, the division of labor is enhanced. Some goods are then produced for foreign trade because there is a demand for them from abroad. From a national point of view, these goods are "surplus produce," as they are not sold or consumed domestically. In this context, the phrase "no demand," which Smith sometimes uses in conjunction with surplus produce, has to be understood.¹¹ In the case of foreign trade, it always refers to the point of view of the nation. Smith equates "the surplus part both of the rude and manufactured produce" with that part "for which there is no demand at home" (WN III.i.7). The phrase "no demand" does not mean that there is an overproduction, but refers solely to domestic demand and to the term "surplus" as described here. Thus, the surplus would not be produced in any case, that is, even without foreign trade. If there was no overall demand for a commodity, it "would never be produced" (WN II.v.5). A surplus is produced only because there is a foreign

10. See also WN I.iv.1. Smith uses the terms "superfluities" and "surplus" in relation to the division of labor already in his earlier *Lectures on Jurisprudence* (LJ) and in the *Early Draft of Part of the Wealth of Nations* (ED) (see, e.g., LJ(A) vi.47, LJ(B) 220, and ED 25). The meanings of the terms "superfluity" and "surplus" are not limited to the division of labor in Smith's writings. Luxury goods, i.e., goods that are not necessities, especially diamonds, gold, and silver, are also described as superfluities (e.g., WN I.xi.e.38, I.xi.g.28, I.xi.m.18–19, I.xi.n.21, and V.ii.k.7). Smith uses the term "surplus" in several other contexts; e.g., he describes the difference between the rent and the necessary expenditure of the landlord as surplus (e.g., WN I.viii.19). The difference between profits and the necessary expenditure of the capital owner, which Smith labels "neat or clear profit" (WN I.ix.18), is also described as a surplus (see also WN I.viii.20). But these alternative uses are not significant for this article.

11. Smith uses the phrase "no demand" in the context of surplus produce once for domestic trade (WN II.v.5) and twice for foreign trade (WN III.i.7 and III.i.31).

market. These commodities did not exist before foreign trade was established (see especially *WN* II.v). Thus, when Smith uses the terms “surplus produce” and “superfluities” in relation to foreign trade, he merely refers to exports. Elmslie and Sedgley (2002, 718) state that they “count 40 times in the *Wealth* where Smith uses the term surplus as synonymous with exports.”¹²

As a consequence, if the demand for some goods collapses or the extent of the market is decreased for another reason, those surplus products for which there is no longer an effective demand will not be produced any more. This is again true for every kind of exchange, including foreign trade: “Those materials are a part of the surplus produce of those countries which, unless it was annually exchanged for something which is in demand there, would be of no value, and would soon cease to be produced” (*WN* II.v.17).

It is not surprising that Smith himself does not speak of vent-for-surplus, because in his theory there is no surplus that needs a vent. Smith’s notion of “surplus produce” is not dependent on unemployed resources, inelastic demand, specificity of resources, or other presumptions. Neither is it opposed to his economic theory of natural liberty. When he talks of “surplus produce” he has neither “a surplus productive capacity in an isolated economy,” as Myint (1958, 323) alleges, nor overproduction in mind. Rather, he writes of “super-abundance” when he refers to unusable goods, that is, goods that have no value and are thrown away. Even in the paragraph on which Heinz Kurz mainly relies for his joint-product interpretation (see Kurz 1990, 1992), Smith speaks first of a superabundance of those products, because “a great part of them is thrown away as useless” and is therefore “of little or no value” (*WN* I.xi.c.3). But as soon as those goods—in Smith’s example skins of animals—are traded with other nations, they are described as surplus products: “the Europeans, with whom they now exchange their surplus peltry, for blankets, fire-arms, and brandy, which gives it some value” (*WN* I.xi.c.4). Thus, as soon as they are tradable and have a value, they stop being superabundant and are surplus products instead. This example is, however, the only time Smith argues that a super-abundant produce becomes a tradable produce as the result of foreign trade. In *WN* I.xi, Smith is concerned with rent, not with foreign trade. Moreover, he describes in this example “nations of hunters and shepherds” and this cannot be seen as a general rule for commercial societies.

12. This interpretation is also suggested by Arthur Bloomfield (1975, 460), but he does not pursue it any further and even discards it.

The depiction of foreign trade as an exchange of surplus produce or superfluities is not peculiar to Smith but was common in his day. Dudley North (1691, 2) states that “trade is nothing else but a Commutation of Superfluities.” Henry Martin ([1701] 1954, 69) writes that “by such an universal Freedom of Trade, our Superfluities wou’d be multiply’d, our exportations wou’d be enlarg’d, our Bullion wou’d be increas’d, and the more Money wou’d be still imploy’d in Trade” (see also 47, 56). William Blake ([1810] 1857, 7) notes, “In the commercial dealings which take place between any two nations, the surplus produce of the one will be exchanged for the surplus produce of the other.” James Syme (1821, 291) says that “the only use of commerce is to exchange the surplus produce of one country for the surplus produce of other countries” (see also 24–26, 315–16). Others who use those terms in this sense include Thomas Mun ([1664] 1928, 8), David Fordyce ([1754] 2003, 98), James Steuart ([1767] 1805, 1:158, 2:2), John Wheatley (1803, 103–4), and Smith’s mentor Henry Home (Lord Kames) (Kames 1774, 512).¹³ The description of exchange between two people and of trade inside a nation as an exchange of surpluses was even more common: see, e.g., Hume [1777] 1987, 260–61; James Mill [1821] 2006, 327; and Torrens 1808, 12, 18.

Smith’s Gains from Foreign Trade

The references to “surplus produce” and “superfluities” in relation to foreign trade, therefore, do not justify the assumption of a vent-for-surplus gain. This conclusion is sustained if we reexamine the crucial paragraph quoted at the beginning of this article (*WN* IV.i.31): “Between whatever places foreign trade is carried on, they all of them derive two distinct benefits from it.” In the next sentence, Smith specifies these two benefits: “It carries out that surplus part of the produce of their land and labour for which there is no demand among them, *and* brings back in return for it something else for which there is a demand” (my emphasis). After having discussed how Smith uses the term “surplus produce,” it is obvious that the first benefit consists of exports, while the second benefit in the latter half of the sentence is imports. Hence, exports and imports are Smith’s two distinct benefits from foreign trade.

From a modern perspective, this statement might seem idiosyncratic, but it becomes clear when the context is considered. This paragraph is

13. This list is of course far from complete.

part of book IV of *The Wealth of Nations*, in which Smith criticizes "two different systems of political œconomy" (WN IV.2), namely, mercantilism and physiocracy. His criticism is based on his own theoretical approach, which he outlines in books II and III. He wants to show that both mercantilist and physiocratic policies do not lead to the most beneficial employment of capital for a nation.¹⁴ In chapter I of book IV, Smith deals with mercantilism in general. According to Smith's depiction,¹⁵ mercantilists value exports as the sole gain from trade and only insofar as they lead to specie inflows, while imports might even be harmful. He disagrees with mercantilists for two main reasons: first, the gain from exports does not consist primarily in specie inflows;¹⁶ and second, exports are not the sole benefit from foreign trade, but imports constitute a gain as well.

For Smith, the gains from foreign trade are not substantially different from those of domestic trade, as the discussion of the terms "surplus produce" and "superfluities" in the last section shows. Foreign trade resembles domestic trade (most emphatically in WN IV.v.b.39). However, Smith separates foreign trade from domestic trade in his analysis throughout *The Wealth of Nations*, and the nation is a level of analysis for him. From this perspective, exports and imports can be described as peculiar to foreign trade, even though their beneficial effects resemble the positive effects of domestic trade. They both increase the wealth in a nation, which Smith defines as "the annual produce of the land and labour of the society" (WN Introduction).

14. For the most beneficial employment of capital, which occurs in a *system of natural liberty*, including the role of foreign trade, see especially WN II.v and III.i. To argue, as some have, that Smith introduces a new approach to foreign trade in book IV is not plausible. Robert Blecker (1997, 529), for example, states that "Smith introduced the vent-for-surplus notion in *the very same passage* in which he introduced the market-widening ('productivity') concept, where he considered them together as the 'two distinct benefits' that countries derive from their foreign trade."

15. Smith describes the mercantilist position as follows: "The two principles being established, however, that wealth consisted in gold and silver, and that those metals could be brought into a country which had no mines only by the balance of trade, or by exporting to a greater value than it imported; it necessarily became the great object of political œconomy to diminish as much as possible the importation of foreign goods for home-consumption, and to increase as much as possible the exportation of the produce of domestick industry. Its two great engines for enriching the country, therefore, were restraints upon importation, and encouragements to exportation" (WN IV.i.35). This is a simplified presentation of mercantilist thinkers, but the aim here is to put Smith's paragraph in context. To that end, it is not necessary to give a differentiated discussion of mercantilist positions.

16. Smith starts the paragraph concerned by stating that "the importation of gold and silver is not the principal, much less the sole benefit which a nation derives from its foreign trade" (WN IV.i.31).

To increase wealth, more capital must be accumulated and employed productively, so that there is a quantitative or a qualitative increase in productive labor: “The annual produce of the land and labour of any society can be augmented only in two ways; either, first, by some improvement in the productive powers of the useful labour actually maintained within it; or, secondly, by some increase in the quantity of that labour” (*WN* IV.ix.34; see also *WN* II.iii.32). According to Smith, the wealth of a country is increased by productive labor, while unproductive labor does not produce wealth.¹⁷ Smith argues that an economically progressing society needs a positive “balance of the annual produce and consumption” (see especially *WN* II.iii.14–18, IV.iii.c.15–17). Savings are the basis of capital accumulation in Smith’s theory. Thus, he esteems parsimony and frugality: “Capitals are increased by parsimony, and diminished by prodigality and misconduct” (*WN* II.iii.14). The motive for such behavior by individuals is “their universal, continual, and uninterrupted effort to better their own condition” (*WN* II.iii.6). Thus, capital owners are not interested only in consuming as much as possible, but in order to afford a better future, they forgo immediate consumption. Yet parsimony alone is not enough. Capital owners must also be able to employ their capital profitably; that is, they have to be able to employ productive labor with it. In Smith’s theory, foreign trade is beneficial because it has a positive influence on parsimony and the “good conduct” of people,¹⁸ offers an opportunity to employ capital productively, and improves the productive powers. Thereby, the wealth of a society is increased through foreign trade.

Through imports, some commodities become cheaper, and goods that are not produced domestically become available. More people might be

17. Smith defines productive and unproductive labor in chapter III of book II. As Walter Eltis (1975, 434) shows, Smith’s distinction is not uniform but he gives three different criteria for productive labor: “(i) whether employment produces a profit, (ii) whether employment produces something storable, and (iii) whether a particular kind of employment can be continued indefinitely without new infusions of capital.” But as Eltis rightly notes, the most important difference in Smith’s theory “is between labour that produces and makes available goods *that can be used as capital* and labour that does not” (434), which is also important in our context. Productive labor “produces a value” (*WN* II.iii.1), while unproductive labor does not (see also Trapp 1987, 229–37). The prime example of an unproductive laborer is the menial servant for Smith. However, unproductive labor can be useful and necessary. Doctors, lawyers, and professional soldiers, for instance, are also in this category. It is not a moral but merely an economic categorization by Smith.

18. Foreign trade is even responsible to some degree for “order and good government” and thus “the liberty and security of individuals” (*WN* III.iv.4).

able to buy those commodities.¹⁹ The variety and amount of available goods in a nation is increased. Additionally, capital owners “may purchase an additional stock of materials, tools and provision” abroad that they use in their production, because they are cheaper or not available domestically (*WN* II.ii.33–35). Technological transfer is another positive effect of foreign trade that is aligned to imports: it is a “mutual communication of knowledge and of all sorts of improvements which an extensive commerce from all countries to all countries naturally, or rather necessarily, carries along with it” (*WN* IV.vii.c.80).²⁰ Additionally, imports are beneficial because of the effect of competition on the behavior of domestic capital owners. Foreign competition decreases the chances of domestic monopolies (e.g., *WN* IV.vii.c.102), which Smith sees as an obstacle to economic growth and describes as “a great enemy to good management” (*WN* I.xi.b.5). High profits, that is, profits above the *natural rate*, have “bad effects [on] the country in general.” The most “fatal” effect resulting from insufficient competition is that this “seems every where to destroy that parsimony which in other circumstances is natural to the character of the merchant.”²¹ The result is that “accumulation is thus prevented” and that “the capital of the country, instead of increasing, gradually dwindles away, and the quantity of productive labour maintained in it grows every day less and less” (*WN* IV.vii.c.61). Thus, imports, by being a competition to domestic producers, promote parsimony.

Exports are also beneficial on their own. The international market leads to a higher effective demand for domestic products. Domestic producers are able to enhance the division of labor as a result. The international

19. In the paragraph following the “two distinct benefits,” Smith gives a numerical example of cheaper imports: “When a commodity comes to be sold for a third part of what had been its usual price, not only those who purchased it before can purchase three times their former quantity, but it is brought down to the level of a much greater number of purchasers; perhaps to more than ten, perhaps to more than twenty times the former number” (*WN* IV.i.32).

20. This includes the imitation of foreign commodities, which Smith assesses positively: Merchants, “in order to save the expence of carriage, . . . establish some manufactures of the same kind in their own country” (*WN* III.iii.16).

21. This is especially worrying because “the owners of the great mercantile capitals are necessarily the leaders and conductors of the whole industry of every nation, and their example has a much greater influence upon the manners of the whole industrious part of it than that of any other order of men. If his employer is attentive and parsimonious, the workman is very likely to be so too; but if the master is dissolute and disorderly, the servant who shapes his work according to the pattern which his master prescribes to him, will shape his life too according to the example which he sets him” (*WN* IV.vii.c.61).

demand “encourages them to improve its productive powers, and to augment its annual produce to the utmost, and thereby to increase the real revenue and wealth of the society” (*WN* IV.i.31). It does so not only in the exporting sectors, but in all production sectors, because technological advances might be used in other sectors. Even agricultural production, whose commodities are less a subject of foreign trade for Smith, might improve as a result (see *WN* III.iv). Through foreign trade commodities can be exported profitably. This provides capital owners an opportunity to employ their capital more productively in the production of exports or in trading activities. Without such an opportunity, some capital would either be employed less productively or capital owners would use their income for unproductive labor (e.g., *WN* III.iv.5). In this case, their behavior would be wasteful rather than frugal. Foreign trade promotes parsimony and thus capital accumulation also because it enables productive investment. Related to this, foreign trade offers a channel for surplus capital (e.g., *WN* II.ii.30, 51; IV.vii.c.96). As Smith often states, if capital cannot be employed at home, it could be invested abroad. In this way, domestic capital would still accumulate.

Thereby, imports and exports both lead to cheaper consumption and encourage production, which Smith describes as “the two effects which it is the great business of political œconomy to promote” (*WN* V.i.e.26). Both increase the wealth of a nation. Consequently, Smith argues that the balance of trade is irrelevant for a nation’s prospects. It can be positive or negative for a long period and even in these cases foreign trade will still be beneficial (see, e.g., *WN* IV.iii.c.17). This illustrates that both imports and exports in themselves are beneficial.

Myint’s Misinterpretation

My scrutiny of Smith’s text contradicts Myint’s influential categorization. Smith’s two distinct benefits do not consist of a vent-for-surplus gain and a productivity gain. From the previous examination it ensues that Smith has no vent-for-surplus theory of international trade in the way it is understood nowadays. As to the productivity theory, it is true that foreign trade leads to an increase in the productive powers of labor, according to Smith. This resembles productivity gains from domestic trade. Smith has no separate theory of foreign trade, but foreign trade is embedded in his theory of (domestic) capital accumulation. However, he uses the nation as a level of analysis, and from this point of view foreign trade is beneficial as a result of exports and imports for Smith.

This raises the question, What led Myint to his false interpretation, and why have so many scholars adopted it? First, Myint and others base their categorization not on the sentence naming the two benefits, but on the following sentences in IV.i.31, in which Smith explains how imports and exports are beneficial for a country. Thus, the explanation of the benefits is confused with the benefits themselves. Second, the terms “surplus produce” and “superfluities” are misinterpreted. Their meaning in modern economics differs from Smith’s meaning of the words, that is, as commodities that are exported. However, Myint and others attribute the modern meaning to Smith. A third reason might be that modern economists are used to deriving gains from trade by comparing autarkic or isolated nations with a situation in which international trade is established. Many scholars stress, when discussing Smith’s supposed “vent-for-surplus” approach, that such gains occur only when an autarkic country starts engaging in international trade, as Myint (1958) does in his original contribution.²² Only in such a framework is it understandable to argue that international trade provides “the new effective demand for the output of the surplus resources which would have remained unused in the absence of trade” (Myint 1958, 321) and superfluities in the modern sense might be imaginable. However, Smith assumes that only precommercial societies were really isolated. When discussing foreign trade and its gains, he does not assume two autarkic nations that start trading. Rather, they are already engaged in trade. Smith describes the benefits of ongoing foreign trade that are realized constantly while conducting trade: “These great and important services foreign trade is continually occupied in performing, to all the different countries between which it is carried on” (WN IV.i.31). These benefits are not once-and-for-all, as the vent-for-surplus argument might suggest. Smith does not assume that there is overproduction before trade. The “surplus produce” of a nation is the result of an effective foreign demand. It does not exist prior to trade.

A reason why Myint’s misinterpretation became the standard interpretation of Smith’s gains from trade is its adoption by established scholars. For example, the editors of the influential *Glasgow Edition of the Works and Correspondence of Adam Smith* included a footnote to WN IV.i.31 stating that “the doctrine of ‘vent for surplus’ was widely applied: see, for example, II.v.33, III.i.1. and IV.iii.c.4.” This prominently placed comment gave the vent-for-surplus interpretation legitimacy and reinforced it.

22. Among them are Findlay and Lundahl (1994), Gomes (1987, 2003), Kindleberger (1964), Meier (1994), Negishi (2004), O’Brien (1975), Platteau (1978), and Winch (1965).

Ricardo's and Mill's Criticism

As mentioned above, some scholars argue that Smith's alleged vent-for-surplus theory contradicts his system of natural liberty. Those scholars often invoke David Ricardo and John Stuart Mill for their argument. In the following, the criticism of Ricardo and Mill should be briefly discussed in order to get a better understanding. The aim is not to defend Smith against Ricardo and Mill but to put their criticism in context, because it too is misrepresented. First, they criticize Smith's wording because an overproduction could be inferred from it. Second, they misunderstand Smith when he notes that "a part of the productive labour of the country must cease." Third, the difference between Smith and classical economists in the nineteenth century lies in the assessment of exports. The latter do not see exports as a gain from trade.

Ricardo is seen as the first one who criticized Smith's vent-for-surplus approach. Ricardo, in his *Principles*, comments on WN II.v.33. Before quoting Ricardo's comments, let us recall what Smith writes:

When the produce of any particular branch of industry exceeds what the demand of the country requires, the surplus must be sent abroad, and exchanged for something for which there is a demand at home. Without such exportation, a part of the productive labour of the country must cease, and the value of its annual produce diminish. The land and labour of Great Britain produce generally more corn, woollens, and hard ware, than the demand of the home-market requires. The surplus part of them, therefore, must be sent abroad, and exchanged for something for which there is a demand at home. It is only by means of such exportation, that this surplus can acquire a value sufficient to compensate the labour and expense of producing it.

In response hereto, Ricardo ([1817] 2004, 291n) states the following:

One would be led to think by the above passage, that Adam Smith concluded we were under some necessity of producing a surplus of corn, woollen goods, and hardware, and that the capital which produced them could not be otherwise employed. It is, however, always a matter of choice in what way a capital shall be employed, and therefore there can never, for any length of time, be a surplus of any commodity; for if there were, it would fall below its natural price, and capital would be removed to some more profitable employment. No writer has more satisfactorily and ably shewn than Dr. Smith, the tendency of capital to

move from employments in which the goods produced do not repay by their price the whole expenses, including the ordinary profits, of producing and bringing them to market.²³

Ricardo's quotation appears in a footnote in a chapter headed "Effects of Accumulation on Profits and Interest," which does not deal particularly with foreign trade. Here, Ricardo tries to defend what became known as the law of markets: "M. Say has, however, most satisfactorily shewn, that there is no amount of capital which may not be employed in a country, because demand is only limited by production" (290). His aim is to demonstrate that an overproduction is not possible: "Too much of a particular commodity may be produced, of which there may be such a glut in the market, as not to repay the capital expended on it; but this cannot be the case with respect to all commodities" (292). This is not so much directed against Smith as against Thomas Robert Malthus, who argues that a "general" or "universal glut" is not only possible but likely to appear, which he defines as follows: "A glut is said to be general, when, either from superabundance of supply or diminution of demand, a considerable mass of commodities falls below the elementary costs of production" ([1827] 1986, 113).²⁴ Ricardo vehemently opposes Malthus's position. In this context he criticizes Smith. Here, Ricardo is not concerned with foreign trade but with the impossibility of a general glut. His criticism is aimed at Smith's choice of words, not at the substance of his argument. Ricardo admits that a theory of overproduction is not what Smith had in mind, as he states in the second half of his quotation above.

John Stuart Mill ([1848] 1965, 592) has the same concerns: "The expression, surplus produce, seems to imply that a country is under some kind of necessity of producing the corn or cloth which it exports; so that the portion which it does not itself consume, if not wanted and consumed elsewhere, would either be produced in sheer waste, or if it were

23. This criticism has been repeated by others, e.g., James Angell (1926) and Lionel Robbins (1958).

24. Malthus ([1820] 1986, 254) states that Jean-Baptiste Say "has indeed gone so far as to state that the consumption of a commodity by taking it out of the market diminishes demand, and the production of a commodity proportionably increases it. This doctrine, however, . . . appears to me to be utterly unfounded, and completely to contradict the great principles which regulate supply and demand." Malthus adds that in this respect "M. Say, Mr. Mill, and Mr. Ricardo . . . appear to me to have fallen into some fundamental errors in the view which they have taken of this subject" (255). It is not necessary to give a full account of the debate between Ricardo and Malthus on the possibility of a general glut here. This can be found in MacLachlan 1999 and Sowell 1963.

not produced, the corresponding portion of capital would remain idle.” But he is less indulgent with Smith and calls his approach “entirely erroneous,” because the law of markets prevents surpluses to be produced or capital to remain idle (592–93). Mill argues that Smith’s theory is close to “the fallacy of general over-production” (593), which he ascribes to Malthus and which he vigorously rejects (see especially Mill [1848] 1965, 570–76).

However, Smith never states that there would be a general overproduction or a universal glut if foreign trade ceased, as Ricardo himself points out. Indeed, Smith is quite clear that a general overproduction or underconsumption is not present in his system of natural liberty: “What is annually saved is as regularly consumed as what is annually spent, and nearly in the same time too; but it is consumed by a different set of people” (WN II.iii.18). Of course, Smith did not endorse what became known as the law of markets or reject Malthus’s concept of a general glut explicitly, because both were unknown to him. However, Ricardo and Mill must have feared that phrases such as “surplus must be sent abroad” could be interpreted in a way to support Malthus’s argument, particularly considering that Malthus “professed to interpret Adam Smith as the true prophet” (Stephen 1900, 238), as did Ricardo and Mill themselves.

Second, there seems to be a misunderstanding about what Smith means when he says that “without such exportation, a part of the *productive labour* of the country must cease” (II.v.33; my emphasis; see also II.v.34). Ricardo, Mill, and also modern scholars seem to interpret this as meaning that the ceasing of trade, or more specifically exports, would lead to unemployment of workers and capital. In a comment directed against Smith, Mill ([1848] 1965, 592) notes that if foreign trade ceases, “the labour and capital which had been employed in producing with a view to exportation, would find immediate²⁵ employment in producing those desirable objects which were previously brought from abroad: or, if some of them could not be produced, in producing substitutes for them.” A similar argument can be found in Ricardo’s *Principles* ([1817] 2004, 294–95). However, Smith would agree with this. He does not argue that unemployment will result if foreign trade ceases. Yet, Smith does argue that workers and thus capital would be employed less productively. Here, the differentiation between productive and unproductive employment discussed above becomes crucial.²⁶ If trade ceases, some part of the former productive labor would be

25. Mill deleted the word “immediate” from the third edition onward.

26. Elmslie and Sedgley (2002, 2003) use a similar argument.

reemployed either less productively or turned into unproductive labor. In the worst case, the capital used to produce exports would be employed in the maintenance of unproductive labor, due to a lack of other investment opportunities. In this case, this capital would not add to the wealth of the country at all, and its owner could use it only for “rustick hospitality at home” but not in commerce (WN III.iv.5; see also V.i.g.22). Even if the capital owner could still employ his or her capital in a productive way, it would be in a less productive way than before. In any case, the potential opulence of a nation is reduced. This is most evident when Smith discusses the effects of policies that restrict or terminate foreign trade: the “industry of the country . . . is thus turned away from a more, to a less advantageous employment, and the exchangeable value of its annual produce . . . must necessarily be diminished” (WN IV.ii.12). The quantity of laborers employed remains the same, because it is determined by the quantity of accumulated capital: “The capital of the country remaining the same, the demand for labour will likewise be the same, or very nearly the same, though it may be exerted in different places and for different occupations” (WN IV.ii.42). Thus, Smith does not assume that capital and labor will become unemployed if trade ceases but that they will be employed less productively. Yet besides Mill and Ricardo, many modern interpreters do claim this. Samuel Hollander (1973, 268), for example, comments on WN II.v.33 that “trade absorbs the output of *factors otherwise unemployed*.” Similar, Nerio Naldi (1996, 215) misleadingly omits the word “productive” and writes about “Smith’s statement concerning the fact that *labour must cease* without the exportation of the *domestic surplus*.”

Third, the main difference between nineteenth-century classical economists on the one hand and Smith on the other is their assessment of exports. For Smith, they form a distinct benefit from foreign trade, as do imports. In contrast, the former value only imports as the sole benefit of foreign trade, while exports do not constitute a gain. This view is most clearly depicted by James Mill ([1821] 2006, 275): “When one nation exchanges a part of its commodities for a part of the commodities of another nation, the nation can gain nothing by parting with its commodities; all the gain must consist in what it receives.”²⁷ John Stuart Mill

27. See also pp. 105–25 of James Mill [1807] 2006, in which he states that “the export commerce of Great Britain is productive of no wealth” (118). This is directed mainly against mercantilists in general, who argue that the benefits from trade consist solely of exports, and against William Spence in particular, who writes “that no riches, no increase of national wealth, can in any case be derived from commerce of import” and that “national wealth may, in some cases, be derived from commerce of export” (Spence 1807, 38).

([1848] 1965, 591) holds the same view: “the only direct advantage of foreign commerce consists in the imports,”²⁸ as does Robert Torrens (1808, 49–50, 53). Ricardo ([1820] 2004, 407) also follows this assessment of imports and exports: “It will be of immense importance to buy cheap, that is to say to obtain plenty of commodities for a little value; and inasmuch as foreign trade, and an extensive market, enables them to do this, it is beneficial to the country” (see also Ricardo [1815] 2004, 25–26; and [1817] 2004, 133).²⁹ Exports are necessary to pay for imports. But they do not constitute an additional benefit, as Smith maintains. In a reference to Smith, John Stuart Mill ([1844] 1967, 253) notes that “political economists . . . have occasionally suffered themselves to employ language evincing inattention to the fact, that exports, though unimportant in themselves, are important by their influence on imports.” In this context, John Stuart Mill charges Smith with adhering to “a surviving relic of the Mercantile Theory.” This relic is the view that exports constitute a benefit from foreign trade. This relic is not, as claimed nowadays, a modern vent-for-surplus gain. The modern misinterpretation of Smith’s gains from trade has also led to a misinterpretation of Mill’s criticism of Smith.³⁰ Mill’s charge is directed against Smith’s view that exports are a gain from foreign trade.

3. Conclusion

Myint’s claim that Smith’s two distinct benefits from foreign trade consist first of a vent-for-surplus gain and second of a productivity gain has been widely adopted and it has not been questioned. However, this separation and especially the vent-for-surplus gain have caused a lot of confusion and discussion. Arthur Bloomfield (1975, 472) once called the meaning of Smith’s vent-for-surplus theory a “mystery.” Yet this mystery does not exist in Smith’s writings but is made up by his interpreters. As I discussed in this article, Myint’s categorization is wrong. Smith’s two distinct benefits are imports and exports.

28. See also Mill [1826] 1967, 130; [1844] 1967, 233, 253.

29. The same is true for Ricardo’s ([1817] 2004, 134–36) famous England-Portugal example. Imports constitute the gains, because both nations can save laborers by the respective imported goods (England “gains the labour of 20 Englishmen” and “Portugal gains the labour of 10 Portuguese” [Sraffa 1930, 541]). Exports are not described as beneficial in themselves.

30. Incorrectly, Morales Meoqui (2010, 39–41) ascribes the view that only imports are beneficial while exports constitute the necessary cost of imports to Smith, as does Charles Bastable (1897, 20). Thereby, Morales Meoqui tries to link Smith’s theory of foreign trade to Ricardo and Mill. He completely overlooks the fact that Mill criticizes Smith for maintaining that exports constitute a gain.

Smith has no vent-for-surplus theory in the modern sense. He rather uses the terms "surplus produce" and "superfluities" as a synonym for exchanged goods and in the case of foreign trade, these are exports. With his position on the gains from trade, he differs from both mercantilists and classical economists of the nineteenth century. The latter reject Smith's gains from trade, because they include exports as a distinct gain. This part of Smith's theory is dismissed by John Stuart Mill as a mercantilist relic, a critique which in turn has also been misunderstood by modern scholars.

This does not mean that modern vent-for-surplus theories cannot be a useful tool in modern economics. They have been used in development economics in several studies in an attempt to try to explain the effects of international trade on a previously isolated country exporting primary goods, as was proposed by Myint (e.g., Caves 1965; Drake 1979; Findlay and Lundahl 1994; Fuglie 1991; Smith 1976).³¹ I do not intend to assess these modern approaches in this article. My point is rather that such theories cannot be attributed to Smith and that representatives of modern vent-for-surplus theories should not refer to Smith as their forerunner.³²

Other economists might be better suited as precursors of modern vent-for-surplus theories. Bloomfield (1981, 100) notes that a paragraph of James Maitland (Earl of Lauderdale) could "be regarded as an early anticipation of modern 'vent for surplus models.'"³³ Furthermore, Bloomfield detects "elements of a 'vent for surplus' theory" (101) in Malthus's *Principles of Political Economy*. There is, however, one classical economist who could be better placed as an early forerunner and this is, of all people,

31. In his original contribution, Myint (1958, 326, 330) argues that "the 'vent-for-surplus' theory provides a more effective approach than the comparative-costs theory to the international trade of the underdeveloped countries," the paradigm being "the typical case of a peasant export economy." Later, he suggests that "the vent for surplus theory may be extended on a somewhat different basis to the agricultural surpluses of the advanced countries such as the United States and the EEC countries" (1987b, 804). Gerald Meier (1994, 15) concludes that a vent-for-surplus approach "has helped to illuminate some historical episodes of nineteenth century development." An appraisal of the vent-for-surplus theory by Myint himself can be found in Myint 1987a, 120–23. Marion Johnson (1974) and R. M. Sundrum (1994) discuss the limits of a vent-for-surplus theory, while Barbara Ingham (1979, 1981) criticizes the "neoclassical version of vent for surplus."

32. I do not dispute that Myint's vent-for-surplus theory really was inspired by Smith. However, if it was, this inspiration would be based on a misunderstanding of Smith.

33. Lauderdale (1804, 353) writes "that commerce . . . must be considered as a cause to increase industry; for, by promoting an interchange of commodities betwixt two countries, it becomes a most powerful agent in extending the demand for the commodities of each, enriching the one and the other, by exciting a quantity of industry that would otherwise have remained dormant; but which, when thus brought into activity, augments the production of both."

John Stuart Mill. Under “indirect benefits of commerce” he names what is comparable to modern vent-for-surplus arguments:

There is another consideration, principally applicable to an early stage of industrial advancement. A people may be in a quiescent, indolent, uncultivated state, with all their tastes either fully satisfied or entirely undeveloped, and they may fail to put forth the whole of their productive energies for want of any sufficient object of desire. The opening of a foreign trade, by making them acquainted with new objects, or tempting them by the easier acquisition of things which they had not previously thought attainable, sometimes works a sort of industrial revolution in a country whose resources were previously undeveloped for want of energy and ambition in the people: inducing those who were satisfied with scanty comforts and little work, to work harder for the gratification of their new tastes, and even to save, and accumulate capital, for the still more complete satisfaction of those tastes at a future time. (Mill [1848] 1965, 593–94)

Here, Mill assumes an isolated country without foreign trade that has some un- or underemployed resources. Foreign trade can be beneficial for such a country because it establishes an international demand for goods that can be produced with these existing but unused resources. This idea corresponds to modern vent-for-surplus approaches. Those previously idle resources are used productively because of foreign trade. This might be a surprising conclusion, because Mill is often seen as one of the first who criticized Smith’s vent-for-surplus theory. However, this is entirely compatible with the analysis of this article. As we have seen, Mill criticizes Smith for assuming that exports constitute a gain from foreign trade besides imports, not for bringing forward a vent-for-surplus argument in the modern sense.

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