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ALTERING THE PATTERN OF TRADE IN THE *WEALTH OF NATIONS*: ADAM SMITH AND THE HISTORIOGRAPHY OF INTERNATIONAL TRADE THEORY

BY

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There are three different interpretations of Adam Smith's trade theory in modern literature: first, the neoclassical theory of absolute advantage; second, an interpretation based on increasing returns; third, an interpretation of uneven development. These interpretations come to widely different conclusions, especially considering the development of the pattern of trade in Smith's theory. I discuss how these three interpretations emerged. They do not stem from a more detailed analysis of Smith's works itself but reflect changes within international trade theory. They all result from the fact that economists have imposed nineteenth- and twentieth-century modes of thoughts on Smith's theory, forcing his writings into later-developed theoretical frameworks. In contrast to classical economists in the nineteenth century, these subsequent interpretations misrepresent Smith's trade theory in order to portray him as a forerunner of later theories. The differing interpretations can thus be explained only against the backdrop of the development of international trade theory.

I. INTRODUCTION

Adam Smith is known today as one of the earliest advocates for free international trade. However, there is less agreement about his trade theory, which underlies his support for free trade. Do natural differences among countries lead to international trade or does international trade generate differences among countries? Does international trade increase the wealth of all nations or does it benefit mostly rich countries and lead to

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uneven development? Will all kinds of commodities be traded equally internationally? Surprisingly, very different answers to these questions are attributed to Smith. In today's literature, there are three competing interpretations of his theory.

First, in neoclassical economics, Smith is portrayed as the founder of the theory of absolute advantage. This theory states that each country will specialize in the production of those commodities that it can produce with less cost and in which it has thus an absolute (production) advantage. Once countries start trading, existing resources are reallocated and used more efficiently, increasing global production. As a result of foreign trade, each country will produce only a few commodities. The international trade pattern is determined by existing productivity differences among countries. It is a static theory: there is just a once-off increase in production resulting from specialization. The trade pattern will remain stable unless an exterior influence affects the production of a commodity in one country. In this case, trade pattern and specialization would adjust. This neoclassical interpretation of Smith's theory can be found in many textbooks on international economics[1] as well as in economic encyclopedias and dictionaries (e.g., Goode 2007; Marrewijk 2009; Moon 2001; Rutherford 2013).

The second interpretation of Smith's trade theory is based on increasing returns to scale.[2] Proponents of this interpretation stress their differences from the neoclassical interpretation, and from neoclassical trade theory based on constant returns to scale more broadly. Neoclassical trade theory assumes specialization resulting from existing, exogenously given, differences between countries. In contrast, trade theories based on increasing returns argue that such differences arise mainly as a consequence of trade. Increasing returns and cumulative causation result in a dynamic development, which leads to ever more specialization and, thus, growing differences in the production structures of countries. Specialization is not seen as a once-off process. This approach—that differences result from rather than cause trade—has even been named after Smith. The "Smithian view of specialisation" (Arrow 1979) or "Smithean logic of trade" (Buchanan and Yoon 2002; see also Buchanan and Yoon 2000) are contrasted with the "Ricardian logic," upon which neoclassical trade theory rests. Based on this increasing returns interpretation, some have argued that Smith already anticipated intra-industrial trade, which the traditional theory of comparative advantage could not account for. In intra-industrial trade, countries specialize, due to increasing returns, in similar commodities, which belong to the same industry and differ only slightly with respect to some characteristics.[3]

[1]The following textbooks in English from the last decades should suffice as exemplary cases: Batchelder and Haitani (1981); Carbaugh (2013); Chacholiades (1973, 1981); Cherunilam (2008); Eicher, Mutti, and Turnovsky (2009); Harris (1957); Ingram and Dunn (1993); Koo and Kennedy (2005); Pugel (2004); Salvatore (1987); Södersten (1970); Wasserman and Hultman (1962); Wells (1969); Wexler (1968); Williamson (1983); Wilson (1986); Yarbrough and Yarbrough (2006); Zhang (2008). This interpretation can also be found in textbooks of neighboring disciplines such as development studies (e.g., Mehmet 1999; Sapsford 2008) and business studies (e.g., Peng 2011).

[2]Proponents of the increasing returns interpretation include Bloomfield (1975); Buchanan and Yoon (2002); Chandra (2004); Gomes (1987); Hong (1984); Kibritçioglu (2002); Krugman (1990); Morales Meoqui (2014); Myint (1958, 1977); Negishi (1985, 1989); Rothschild and Sen (2006).

[3]Smith is associated with intra-industrial trade by Blecker (1997); Elmslie and James (1993); Morales Meoqui (2014); Negishi (1985, 1989); Pomfret (1986). Takashi Negishi goes as far as saying that Smith's theory is "a theory of intraindustrial specialization rather than a neoclassical theory of interindustrial specialization" (1985, p. 33).

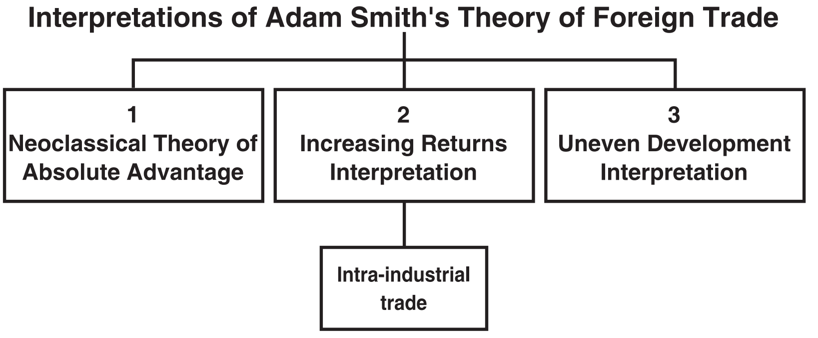

FIGURE 1. Three Interpretations of Adam Smith's Theory of Foreign Trade.

A third interpretation claims that foreign trade in Smith's theory leads to uneven development.[4] This interpretation stresses the dynamic elements and especially cumulative causation. Additionally, it relies on an "asymmetry between manufactures and primary production" (Alam 2016, p. 9), which allegedly makes manufacturing more beneficial for a country, in Smith's theory. Due to an initial backwardness, poor countries are forced to specialize in the production of agricultural commodities, which are "non-dynamic-returns goods" (Milberg and Elmslie 1993). They will experience slow technological development and productivity growth. Rich countries, in contrast, will specialize in the more rewarding manufacturing sector. The corollary is that poor countries will not be able to catch up, being unable to compete with rich countries in manufacturing. The trade pattern is thus determined by the level of a country's opulence compared with that of its trading partners when trade started. Countries with a head start will specialize in manufacturing; countries whose development lags behind will specialize in agriculture. Since specialization leads to more specialization, the gap between rich and poor countries will grow over time, starting "a naturally virtuous and vicious cycle of uneven development" (Elmslie and James 1993, p. 67). Poor countries might still gain absolutely but not relative to rich countries and they are confined to underdevelopment.

To sum up, there are nowadays three distinct interpretations of Smith's trade theory, which are depicted in Figure 1: the *neoclassical theory of absolute advantage*, the *increasing returns interpretation*, and the *uneven development interpretation.* These three interpretations lead to widely different conclusions concerning the effects of trade and the development of trade pattern.

Rather than championing any of these interpretations, I will reconstruct how these three different interpretations emerged. I will argue that their respective emergences are

[4]The uneven development interpretation is championed by Alam (2000, 2016); Darity and Davis (2005); Elmslie (1994); Elmslie and James (1993); and Milberg and Elmslie (1993). Robert A. Blecker (1997) and Farhad Rassekh (1998) agree with this interpretation, while P. Sai-wing Ho (1996, 2016) also hints at it, but he does not state that some countries necessarily specialize in agriculture. Samuel Hollander (1973, pp. 291–292), who is close to the neoclassical interpretation of absolute advantage, also briefly hints at possible uneven development. Nicholas Kaldor (1978, pp. 237–238) argues that Smith's theory would imply such an uneven development conclusion, but that Smith himself does not draw it. The interpretation that some countries have to specialize to their own disadvantage in agricultural production in Smith's theory was already stated by Hermann Roesler (1864, p. 280).

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not the result of a more comprehensive study of Smith's writings but can be explained by the development in international economics. All three interpretations of Smith reflect developments within international trade theory. They impose later modes of thoughts on Smith's theory, thereby distorting and misinterpreting his theory. Even though they differ in the way they misconstrue Smith's theory, they all erroneously ascribe one concept to Smith: an international territorial division of labor—a concept that became the main basis for trade theory only in the nineteenth century. In the next section, I will briefly discuss the development of the pattern of trade in Smith's theory of foreign trade. This discussion is based on more comprehensive studies of the role of trade in Smith's theory of economic development (Schumacher 2016) and the positive part of his trade theory (Schumacher 2018). Then, I will trace how Smith has been (mis)represented in the history of international trade theory, starting with classical economists in the nineteenth century. I will show how later economists in the twentieth century incorporated Smith in their respective historiographies of international trade theory by linking Smith to their own theories. In order to achieve this incorporation, different modes of thought have been imposed on Smith. I will conclude with a discussion of why Smith has been claimed by very different theories.

II. PATTERN OF TRADE IN THE *WEALTH OF NATIONS*

In his *Wealth of Nations (WN)*, Smith embeds foreign trade in his theory of economic progress. Economic progress is led above all by domestic capital accumulation. His theory culminates in the *natural progress of opulence.* According to Smith, capital will be "first, directed to agriculture, afterwards to manufactures, and last of all to foreign commerce" (*WN* III.i.8). Foreign trade ranks at the end of this order because it is "the least productive and most unstable sector of the economy" (Harpham 1984, p. 767). This *natural order* is at the same time the most beneficial development for a country and unfolds best in a *system of natural liberty.*[5] This development is the consequence of the profit and security motives of capital owners (*WN* II.v and III.i) in combination with a falling (domestic) rate of profit resulting from capital accumulation (see especially *WN* I.ix and II.iv).[6] Foreign trade is the result of a certain level of domestic economic development, not its cause. Domestic capital accumulation is the main determinant of the pattern of foreign trade. Smith concludes that the opulence of a country and the volume of its foreign trade are related: "the foreign trade of every country naturally increases in proportion to its wealth" (*WN* IV.vii.c.22).

Besides domestic capital accumulation, three further aspects play a major role for the international trade pattern in Smith's theory: transport costs, geographical factors, and the preferences of capital owners.[7] First, transport costs relative to the value of the transported commodity are highest for agricultural commodities, followed by coarser

[5] If a country departs from a system of natural liberty, it can distort this natural order. At the extreme, policies can even lead to an "unnatural and retrograde order." However, the "natural course of things" has to take place "in some degree in every [economically developing] society" (*WN* III.i.8–9), according to Smith.

[6] On the falling rate of profit in Smith's theory, see Schumacher (2018, p. 7); Tsoulfidis and Paitaridis (2012); Tucker (1960, pp. 49–73); and Verdera (1992).

[7] A more detailed discussion of these aspects can be found in Schumacher (2018, pp. 5–13).

manufactured commodities, while they are lowest for sophisticated manufactured commodities. Therefore, it is mainly manufactured commodities that are traded internationally (*WN* IV.ix.41), while agricultural commodities are rarely the subject of foreign trade, according to Smith. Second, geographical factors, "the nature of its soil, climate, and situation" (*WN* I.ix.15), might give countries an unbridgeable disadvantage in the production of certain commodities. This, however, plays a role only for some agricultural and primary commodities, such as Scottish viticulture (*WN* IV.ii.15). Third, capital owners prefer to invest their capital in close vicinity under their supervision because of quicker returns and greater security of their investments. This gives domestic capital owners an incentive to emulate manufactured commodities from abroad that are in demand domestically. Through such emulation, "the merchants, in order to save the expence of carriage, naturally endeavoured to establish some manufactures of the same kind in their own country" (*WN* III.iii.16).

These considerations lead to the conclusion that international trade will take place mostly among the most developed countries trading manufactured commodities. The volume of trade between two countries is positively correlated to their level of capital accumulation, their market sizes, and their geographical nearness—or, in Smith's words, the trade volume is "in proportion to the wealth, population and proximity of the respective countries" (*WN* IV.iii.c.12).[8] Smith argues that agricultural commodities, such as corn and meat, will barely be traded internationally and even in free trade could barely affect a domestic market for such goods, except for small countries (e.g., *WN* III.iii.20; IV.ii.16–20; IV.v.b.28–30). This is why he assumes that most countries are mostly self-sufficient in terms of food and coarse manufactured commodities such as "cloathing and houshold furniture" (*WN* III.iii.17). Less developed countries are not excluded from foreign trade, but foreign trade is less important to them, because their capital owners have better investment opportunities domestically and because they produce fewer commodities that are suitable for foreign trade. Developed countries, emulating each other, are likely to produce, over time, similar commodities, which is why Smith frequently argues that foreign trade increases competition. In fact, increased competition is arguably the greatest benefit of foreign trade, according to Smith, above all because it increases parsimony[9] and counters the "monopolizing spirit" (*WN* IV.iii.c.9) of merchants and manufacturers, who "dread the competition of the skill and activity of those of the other" (*WN* IV.iii.c.13).[10]

In his assessment of the benefits of trade, Smith followed the so-called eighteenth-century rule (see especially *WN* IV.ii.12), which Jacob Viner defined as "the rule … that it pays to import commodities from abroad whenever they can be obtained in exchange for exports at a smaller real cost than their production at home would entail" (Viner 1937, p. 440). However, in contrast to other writers, Smith did not derive from this observation

[8]A similar interpretation has recently been propounded by Bruce Elmslie, who links Smith's theory of foreign trade to modern gravity models of international trade (Elmslie 2018).

[9]For Smith, parsimony "is the immediate cause of the increase of capital. Industry, indeed, provides the subject which parsimony accumulates. But whatever industry might acquire, if parsimony did not save and store up, the capital would never be the greater" (*WN* II.iii.16).

[10]Smith did not assume perfect competition, but he rather had a "behavioral" concept of competition (Blaug 2007, p. 188). On the potential disastrous aspects of the "monopolizing spirit" in Smith's thought, see Paganelli and Schumacher (2018).

a theory of international specialization. At least in the long run, Smith predicts that most commodities will be produced in most countries. Economic development leads thus to a diversification of production, not to specialization—neither complete nor partial specialization. Foreign trade will not result in countries specializing in different sectors of production, according to Smith's theory. Thus, no country will specialize in the long run in agricultural commodities or in manufacturing. Neither will there be a specialization in different manufacturing commodities. Rather, each economically developed country will diversify and produce most commodities. Only certain primary and agricultural goods, which can be produced profitably only in some countries (or even in just a single country) due to geographical factors, form an exception. With the exception of such commodities, which constitute only a small part of international trade, foreign trade will not lead to international specialization, according to Smith's theory. Rather than becoming a specialist, a developed country will become a jack of all trades. Countries might produce and trade different commodities with each other, but this is mainly due to their different levels of economic development. This entails that Smith's theory of foreign trade is based neither on the Smithian nor on the Ricardian logic of trade, which I discussed in the introduction. The label "Smithian logic" is a misnomer when it comes to foreign trade.

However, Smith is often associated foremost with the division of labor, which is at least partly due to its prominent place in the first chapters of Smith's *Wealth of Nations.* And he does refer to the division of labor and technological progress in the context of foreign trade. But Smith uses the division of labor solely in terms of a *mechanical division of labor*, not a *territorial division of labor*, to use a categorization introduced by Robert Torrens (1808, p. 44; see also 1821, pp. 248–250). Smith argues that the increase in "the productive powers of labour," which results from an enhanced division of labor, "is owing to three different circumstances; first, to the increase of dexterity in every particular workman; secondly, to the saving of the time which is commonly lost in passing from one species of work to another; and lastly, to the invention of a great number of machines which facilitate and abridge labour, and enable one man to do the work of many" (*WN* I.i.5). He famously illustrates this productivity increase with an example of a pin factory (*WN* I.i.3). In Smith's theory, the division of labor is "limited by the extent of the market." Foreign trade increases the market and enhances division of labor: "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" (*WN* IV.i.31). Producers can increase their production and enhance the division of labor inside their respective production processes, exploiting the "three different circumstances" and increasing productivity. Hence, it is the mechanical division of labor that is affected by foreign trade, in Smith's theory. In contrast, the territorial division of labor is largely absent in his account of foreign trade—with the exception of some primary and agricultural goods owing to certain geographical factors.

This is why Smith stresses emulation as a benefit from foreign trade, which applies especially for rich countries producing manufacturing commodities. He exemplifies this using China, which, according to Smith, is one of wealthiest countries "that ever were in the world" (*WN* II.v.22). Because of its large domestic market, China reached its "very high degree of opulence" despite largely sealing itself off from foreign trade (*WN* III.i.7; see also *WN* I.ix.15; IV.ix.40). Although it has highly developed agricultural and manufacturing sectors, China could benefit from opening up to foreign trade. It would be able to learn from and then emulate the manufacturing industries abroad (*WN* IV.

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ix.41), benefitting from technological transfer and increasing its mechanical division of labor and thus its labor productivity. The reason that rich countries benefit most from technological transfer is that they have a developed manufacturing sector, and the division of labor, according to Smith, can be enhanced much further in manufacturing compared with agriculture, which "does not admit of so many subdivisions of labour, nor of so complete a separation of one business from another, as manufactures" (*WN* I.i.4). This is another reason why foreign trade is less important for less developed countries, which do not have large manufactures yet. They can benefit less from technological transfer. In contrast, foreign trade is important for rich countries, because without it, the mechanical division of labor and thus the productive powers of labor could not be brought to their full potential. Smith argues that the "perfection of manufacturing industry" (*WN* IV.ix.41) requires foreign trade and international demand. There is a circular causation: foreign trade depends mainly on sophisticated manufactured commodities and the improvement of manufacturing depends on foreign trade. For this reason, foreign trade is more important for small countries than for large countries with large domestic markets. Their small domestic markets allow only a relatively small low division of labor and their manufacturing sectors "generally require the support of foreign trade" (*WN* IV.ix.41). Foreign trade enables small countries to enhance their mechanical division of labor as much as possible and thus to produce commodities they could not produce without a foreign market. In this way, a small country will diversify, not specialize, as a result of foreign trade.

III. ADAM SMITH AND THE HISTORY OF INTERNATIONAL TRADE THEORY

In contrast to Smith, succeeding classical economists began to conceive international trade in terms of a territorial division of labor. Torrens argues that foreign trade enhances both the mechanical as well as the territorial division of labor and both make foreign trade beneficial, but he discusses the latter at greater length (1808, pp. 44–49; 1821, pp. 248–289). Successors of Torrens dropped the mechanical division of labor mostly from their theories of foreign trade. David Ricardo stresses the importance of the territorial division, arguing that more commodities can be produced "by the better distribution of labour, by each country producing those commodities for which by its situation, its climate, and its other natural or artificial advantages, it is adapted" ([1817] 2004, p. 132). Most nineteenth-century classical economists followed this view of foreign trade (see, e.g., Hodgskin 1827, pp. 142–143; McCulloch 1825, pp. 119–127; McCulloch 1833; Senior 1836, pp. 159–162).[11] As John H. Williams notes, classical economists in the nineteenth century used "a theory of benefits from territorial division of labour," whereby national specialization became "the characteristic feature and the

[11] James Mill had already discussed trade mainly in terms of national specialization ([1807] 2006, pp. 109–110, 149, 155–156; [1821] 2006, pp. 270–274). Another influential classical economist, John Stuart Mill, does not discuss the difference between mechanical and territorial division of labor explicitly in connection to international trade, but he implicitly refers to both while discussing the benefits from foreign trade. The territorial division of labor is depicted as "the direct benefit of commerce" ([1848] 1965, pp. 590–591), while the mechanical division of labor is seen as one of the "indirect benefits of commerce" ([1848] 1965, p. 593).

root idea of international trade" (1929, p. 203). The mechanical division of labor was precluded from foreign trade theory. John E. Cairnes, for example, argues that the mechanical division of labor is in most cases already extended as far as possible by domestic trade, with the result that foreign trade can only increase the territorial division (1874, pp. 356–361). Only in small countries, in which the "population is very sparse" (Cairnes 1874, p. 359), can the mechanical division of labor be enhanced by foreign trade. This is only an exceptional case: "In the main, however, it would seem that this cause does not go for very much in international commerce" (Cairnes 1874, p. 361). Foreign trade became thus synonymous with an *international division of labor* understood solely in terms of a territorial (or geographical) division of labor. Countries were seen as being complementary to each other due to their inherent differences. Additionally, classical economists started treating foreign trade as a topic that could be separated from overall economic theory, which Smith did not.

Classical economists were usually very sympathetic towards Smith, as whose heirs they saw themselves. They praised Smith for his advocacy of free trade but, using their own theories as yardsticks, they criticized Smith for his omission of international specialization and the territorial division of labor.[12] Torrens refers to Smith when describing the mechanical division of labor and adds that "it is not in mechanical operations alone that the division of employment augments the powers of industry" (1821, p. 156), thereby implying Smith's omission of the territorial division. More explicitly, Nassau Senior, when discussing the territorial division of labor, notices that "Adam Smith, though he has alluded to it, has not prominently stated" it (1836, p. 160). John Stuart Mill, after having discussed Smith's three advantages from the division of labor in general, notices that "[t]he greatest advantage (next to the dexterity of the workmen) … is one not mentioned by Adam Smith," namely, "the more economical distribution of labour, by classing the work-people according to their capacity" ([1848] 1965, p. 128). Edwin Cannan argues that Smith "tuck[ed] away the advantage arising from 'territorial division of labour'" (1929, p. 98) and that he "omitted altogether the economy of tools and the possibility of localising industries so as to get the most good from different qualities of different places" (1929, p. 96).[13] Others followed Torrens by implying that Smith's theory does not include a territorial division of labor. These authors describe Smith's advantages from the division of labor and then add that there is another kind of division of labor, the territorial division (e.g., McCulloch 1825, pp. 85–95, 119–127; Gide 1904, pp. 174–176; Lutz, Foote, and Stanton 1933, pp. 70–78). Consequently, Torrens was described by Langford Lovell Price as having "bestowed on Free Trade the significant title of 'territorial division of labour'" (1902, p. 314)—not Smith, as is often done today.

Neoclassical Theory of Absolute Advantage

The conception of foreign trade as a territorial division of labor, which classical economists in the nineteenth century had developed, was adopted by subsequent

[12]Classical economists were equally critical of Smith's conception of the gains from trade (Schumacher 2015, pp. 592–596).

[13]Earlier, and before his profound engagement with Smith, Cannan (1894, p. 47) already noted that Smith did not list the territorial division among the advantages of the division of labor, but Cannan then claimed unconvincingly that Smith nevertheless "fully recognised" it in foreign trade.

economists.[14] Neoclassical economists preclude the mechanical division of labor from international trade, arguing that—with the exception of very small countries—it was already extended as far as possible by domestic trade and could not be enhanced much further by international trade (e.g., Haberler [1933] 1950, pp. 130–131; Harrod 1933, pp. 11–12). International trade is understood merely in terms of a "specialisation by national areas" (Haberler [1933] 1950, p. 130).[15] Each country will specialize in the production of certain commodities, leading to an international territorial division of labor. International trade is seen as beneficial only because it exploits existing differences between countries.

In contrast to classical economists, however, neoclassical economists reinterpreted Smith's trade theory. They started asserting that Smith perceived foreign trade mainly or even only as a territorial division of labor. This reinterpretation of Smith's theory can be traced back to the early twentieth century, when neoclassical economics had been established. Smith was linked, at first, to the territorial division of labor in works on international trade (e.g., Angas 1935; Angell 1926; Killough 1938; Price 1902; Young 1938) as well as on the history of economic thought (e.g., Gide and Rist [1915] 2000; Surányi-Unger 1923).[16] These depictions often implied a theory of absolute advantages, but others went further and attributed this theory explicitly to Smith (e.g., Bickel 1926; Kobatsch 1907; Litman 1923; Viner 1932, 1937). The concept of absolute advantage had been introduced by classical economists to explain the concept of comparative advantage. But in contrast to neoclassical economists, classical economists did not attribute this concept to Smith (Schumacher 2012, p. 71).

The mechanical division of labor, neglected by neoclassical trade theory, is erased in this depiction of Smith. It is even argued that in Smith's theory, "technologies in [the trading] countries are fixed" (Zhang 2008, p. 24)—excluding any possibility of an enhancement of the mechanical division of labor. Analogous to neoclassical trade theory, Smith's theory is depicted as relying solely on the territorial division of labor. As a result, the neoclassical interpretation comes to opposing conclusions concerning the pattern of trade compared with Smith himself. The most obvious instance is the claim that some countries will specialize in agricultural commodities. Many textbooks use a numerical example with two countries and two commodities to illustrate Smith's theory of absolute advantage. These examples often include an agricultural and a manufactured

[14]The following list of late nineteenth-century and early twentieth-century economists should suffice to illustrate this development: Bastable (1897, 1899); Brown (1914); Bye (1924); Bye and Hewett (1928); Cannan (1902); Carver and Carmichael (1929); Clay (1918); Deibler (1929); Ely et al. (1916); Garver and Hansen (1928); Gide (1904); Griffin (1924); Hobson (1904); Horn (1935); Kidd (1921); Laveleye (1884); Magee (1922); Seager (1913); Taussig (1911); Thompson (1928).

[15]The equalization of the mechanical and the territorial division of labor with domestic and foreign trade, respectively, was not maintained by all. Many argued that the territorial division of labor also applied to domestic trade between different regions. On the other hand, some included the mechanical division of labor in foreign trade. But it was always perceived as an afterthought to the territorial division of labor, meaning that the territorial division of labor leads to specialization and this specialization might enhance the mechanical division of labor (e.g., Bastable 1897, pp. 19–22; Bastable 1899, pp. 16–17; Gide 1904, pp. 176, 301–307; Taussig 1911, pp. 45–48; Whale 1932, pp. 107–108).

[16]Neoclassical economists, generally sympathetic to Smith, were not the only ones interpreting Smith in this way. Economists critical of Smith in the German-speaking world also interpreted Smith's theory of foreign trade as being based mainly or only on a territorial division of labor (e.g., Eßlen 1925; Eulenburg 1929; Roesler 1864; Spann 1922).

commodity showing that one country will specialize in the agricultural commodity while the other specializes in the manufactured commodity.[17] In contrast, Smith does not assume that some countries specialize in agriculture. Rather, independent of ongoing foreign trade, poorer agricultural countries will in due time accumulate capital and establish a manufacturing sector.

Moreover, the neoclassical interpretation assumes that existing resources are reallocated more efficiently worldwide due to international specialization. There are no quantitative or qualitative changes of those resources. This leads to the corollary that trade volumes will be largest between the most dissimilar countries, because the possible gains from a reallocation of resources are greatest in this case. This also supposes that foreign trade is independent of domestic development and that differences between countries are solely responsible for the pattern of international trade. In contrast, Smith does not emphasize the static, once-off reallocation of existing resources in the context of foreign trade. As Mark Blaug rightly notes, the idea of "'static efficiency' … is foreign to Adam Smith," who instead assumed "dynamic progress" (2007, p. 190). Foreign trade influences capital accumulation and the mechanical division of labor, thereby changing the quantity and quality of productive resources. Furthermore, the pattern of foreign trade is determined by domestic economic development and not independent of it. In contrast to the neoclassical interpretation, Smith assumes trade volumes to be largest between highly developed countries, which have similar production structures.

Additionally, the neoclassical interpretation overlooks the importance of transport costs in Smith's theory. In fact, the assumption that there are no transport costs is ascribed to Smith, either explicitly or implicitly. This further misrepresents the pattern of trade and its development in the *Wealth of Nations.* In contrast to the neoclassical interpretation, Smith stresses the difference in transport costs between agricultural and manufactured commodities, which has important implications for foreign trade in his theory.

Smith's own theory is largely neglected in the neoclassical interpretation. Capital accumulation, transport costs, and preferences of capital owners, which play a central role for the pattern of trade in Smith's theory, are ignored. Instead, neoclassical economists imposed nineteenth-century modes of thought, to which they themselves adhered, on Smith's trade theory—modes of thought that contradict Smith's own theory. In this way, it became possible to portray Smith as an early predecessor of neoclassical trade theory.[18]

[17]Out of the textbooks listed in footnote 1, the following contain numerical examples that include one agricultural commodity: Chacholiades (1981); Cherunilam (2008, p. 124); Eicher, Mutti, and Turnovsky (2009); Koo and Kennedy (2005); Marrewijk (2009, pp. 1–2); Mehmet (1999); Pugel (2004); Sapsford (2008, p. 76); Salvatore (1987, pp. 16–17); Williamson (1983, pp. 21–25); Zhang (2008).

[18]In neoclassical economics, the Heckscher–Ohlin model became the standard theoretical framework. It explains comparative advantage through differing relative factor endowments. It seems consequential that after its establishment, some have argued that Smith already used factor endowments to explain the pattern of trade (Hollander 1973, pp. 278, 283–284; Maneschi 1998, p. 48; O'Brien 1975, p. 171; Viner 1937, p. 503) and that he even anticipated to some degree the Heckscher–Ohlin model itself (Bloomfield 1975; Morales Meoqui 2014, pp. 32–34; Myint 1977; Power 1987, pp. 294–295). To connect Smith to the Heckscher–Ohlin model is equally misleading. It misinterprets Smith by imposing the same neoclassical modes of thought on Smith. Additionally, the modern concept of (natural) factor endowment is not used by Smith.

Increasing Returns Interpretation

Neoclassical trade models based on constant returns to scale came under attack in the 1970s and 1980s from within neoclassical economics. Empirically, the deficiency of neoclassical trade theory became most obvious by the large share of intra-industry trade of world trade, which it could not explain. As a result, the new trade theory emerged, which puts non-static explanations such as increasing returns to scale at its center. That increasing returns might play a role in international trade was acknowledged earlier, but they were ignored in economic models "for the simple reason that the theoretical difficulties are considerable, and it is not generally agreed how they can be incorporated into a model of general equilibrium or whether they are at all compatible with the assumptions of perfect competition" (Chipman 1965, p. 737). Once the "principal obstacle to formal modeling of increasing returns in trade" (Krugman 1990, p. 4) was overcome by the development of new mathematical concepts, increasing returns were integrated into neoclassical trade models. Based on increasing returns, the new trade theory predicts geographical agglomeration and thus specialization as a result of international trade.

Smith had already been connected with the concept of increasing returns earlier, most famously by Allyn Young (1928), but not in the context of international trade. Paul Samuelson stated that Smith "made *increasing returns* an important cause for trade" (1949, p. 195; see also 1969, p. 4), but this was only an incidental remark. More influential, Hla Myint, referring to Young, argues that "increasing returns and economic development" are an inseparable part of Smith's international trade theory. He contrasts the "Adam Smithian process of specialisation" and its "dynamic force" with the static "comparative-costs doctrine" (Myint 1958, pp. 318–319), stressing the link between trade and growth. However, the view that Smith's trade theory is based on increasing returns to scale gained wider acceptance only a few decades later, after the new trade theory had been established, which gave increasing returns a new prominence. This is not to say that the new trade theory was inspired by Smith in the first place. Rather, only after the consolidation of the new trade theory did the increasing returns interpretation gain wider acceptance. Thus, Smith could be portrayed as a forerunner of the new trade theory. Intra-industrial trade became the focus of the new trade theory, and Smith was presented as a forerunner of this concept as well, by making the argument that Smith already assumed that countries specialize in differentiated commodities of the same industry.

Although the increasing returns interpretation does to some extent reintroduce the mechanical division of labor into Smith's trade theory, this happens only as an afterthought to the territorial division of labor. It is only due to the enhanced territorial division of labor that the mechanical division of labor in the form of increasing returns can be enhanced. Foreign trade starts a dynamic process of specialization, whereby initial differences between countries are reinforced, making a territorial division of labor evermore beneficial. The production structures of countries become more and more dissimilar, according to the increasing returns interpretation. In contrast, Smith assumes that, eventually, the production structures of countries will converge and international competition increases. Kenneth J. Arrow, referring to increasing returns, notes that "Smith never realized that there is something of a contradiction between this proposition and his basic economic theory of competition" (1979, p. 156). This illustrates how the increasing returns interpretation misunderstands Smith's theory. Arrow's claim is indeed true for the increasing returns interpretation itself.[19] If all countries specialized fully in the production of different commodities, there would be no international competition at all. And even partial specialization would decrease international competition. Specialization would thus lead to less, not more, competition. This contradiction, however, does not occur in Smith's theory, because he does not assume international specialization. Rather, he assumes that countries will emulate each other and produce similar commodities, increasing not only the mechanical division of labor but also international competition. As Smith frequently argues, domestic producers, especially in manufacturing, face stiffer competition as a result of foreign trade. Apart from this, the identification of Smith's division of labor with the concept of increasing returns to scale is deficient. The concept of increasing returns merely implies that when all factor inputs are increased simultaneously by an identical proportion, output increases in a greater proportion. Smith's concept of the (mechanical) division of labor is much more sophisticated and complex. Regarding intra-industrial trade, Smith does not address this modern concept, which, of course, had to be alien to someone writing at the onset of the Industrial Revolution. Additionally, intra-industrial trade theory suggests that countries specialize in different kinds of commodities of the same industry. This is not compatible with Smith's own theory.

To sum up, proponents of the increasing returns interpretation reinterpreted Smith's trade theory once more. This reinterpretation is not the result of an improved textual analysis of Smith's writings by a new generation of scholars but rather a reaction to developments in international trade theory. Similar to the neoclassical interpretation, the crucial role of capital accumulation, transport costs, and preferences of capital owners in Smith's theory are ignored. The increasing returns interpretation imposed twentieth-century modes of thought on Smith's trade theory, which, however, are not consistent with Smith's own theory. The emergence and spread of the increasing returns interpretation, and also the attribution of intra-industrial trade to Smith, can be explained only by the development of trade theory, namely, by the emergence and spread of the new trade theory, in which increasing returns play a central role.[20]

Uneven Development Interpretation

The third interpretation, the uneven development interpretation, also rests on a territorial division of labor, arguing that poor countries have to specialize in agricultural production while rich countries are able to specialize in the more beneficial manufacturing production. However, Smith does not assume that some less developed countries will have to specialize in agriculture. According to him, they will introduce manufacturing once they have accumulated sufficient capital domestically. To argue that Smith failed to

[19]The accusation that international specialization in Smith's theory would lead to a decrease of competition can already be found in Roesler (1864).

[20]I am interested here only in the way Smith is presented in the increasing returns interpretation. I am not covering all strands and developments within the new trade theory. An anonymous referee pointed out that some strands stress that the increased competition each firm faces is the most important gain from international trade. This is indeed a similarity to Smith's own theory. However, this comparison is not made by proponents of the increasing returns interpretation, and, in contrast to Smith's theory, the increased competition a firm faces is mostly due to domestic competitors.

"indicate the gains … from specialization in agriculture" (Elmslie and James 1993, p. 69) for poorer countries misses the point, because there is no such specialization in Smith's theory. Additionally, it is incorrect to assume that agriculture is the basis for relative impoverishment in Smith's theory. Smith's natural progress of opulence stresses the importance of agriculture for economic development. Capital employed in agriculture is the most beneficial employment for a country and thus "the prime contributor to wealth" (Tribe 2006, p. 64). This is because "[i]n agriculture too nature labours along with man; and though her labour costs no expence, its produce has its value" (*WN* II.v.12). The prospects of thriving agricultural countries are not desperate but bright. This can be illustrated by Smith's discussion of North America: "It has been the principal cause of the rapid progress of our American colonies towards wealth and greatness, that almost their whole capitals have hitherto been employed in agriculture" (*WN* II.v.21). These colonies are the "example of a 'progressive' society par excellence" (Winch 1996, p. 150) for Smith, even though they have not yet established any significant manufacturing (see also *WN* I.viii.23, I.ix.11, III.iv.19).[21] The accumulation of capital will eventually lead to the establishment of a manufacturing sector and of foreign trade: "Each of those different branches of trade, however, is not only advantageous, but necessary and unavoidable, when the course of things, without any constraint or violence, naturally introduces it" (*WN* II.v.32).

The uneven development interpretation entails that poor countries, which have to specialize in agriculture, will de-industrialize if they had some manufacturing before they started trading (Elmslie 1994, p. 258; Rassekh 1998, p. 93)—an argument directly contradicting Smith's natural progress of opulence. An obvious remedy for these suggested developments would be trade restrictions that favor domestic industry such as infant industry protection. Unsurprisingly, some proponents of this interpretation argue that this is an "implication of his theory" (Darity and Davis 2005, pp. 147–148; see also Alam 2016, p. 10; and Elmslie and James 1993, p. 69). However, Smith, in accordance with his theory, argues against infant industry protection (e.g., *WN* II.v.21 and IV.ii.13-4).

The uneven development interpretation, as the two other interpretations, ignores the role of capital accumulation, transport costs, and preferences of capital owners in Smith's theory. It is true, however, that in Smith's theory, countries do not develop economically in lockstep. Different levels of domestic capital accumulation will initially increase the economic inequality between countries and thus lead to a diverging gap between them. However, this gap is not caused by foreign trade, in Smith's theory. Foreign trade in Smith's theory is the result of economic development, not the reason for underdevelopment. Poor countries will not remain backward as a result of foreign trade. Rather, the initially growing gap between rich and poor countries will be narrowed in the long run, since the economic growth of a country will eventually slow down and come to a halt, in Smith's theory (Schumacher 2016). In contrast, the uneven development interpretation assumes an indefinite divergence with international trade as the sole culprit.

[21]Proponents of the uneven development interpretation have noticed that these paragraphs do not correspond to their interpretation. They often declare the North American colonies as exceptions. Some have proposed an unconvincing classification between countries that have an absolute advantage in agriculture facing a bright future, such as the North American colonies, and countries that have a comparative advantage in agriculture whose future is less bright (Elmslie and James 1993, p. 68; Elmslie 1994, p. 268n).

The uneven development interpretation has to be explained in the light of the emergence of uneven development theories, which were brought forward by development economists and which stress especially cumulative causation and path-dependence. Development economics as a subject focusing on developing countries took off after the Second World War. One of the questions raised was why some countries remained underdeveloped over a long period. Dependency theory, unequal exchange theories, and other theories stress endogenous reasons for uneven development. It is not surprising that the uneven development interpretation of Smith's trade theory has its origin in development economics, which is often critical of neoclassical theory. Its proponents are often economists who were at least partly influenced by uneven development theories rather than by neoclassical economics. It was through the spectacles of such theories that they read Smith. The claim that Smith's theory of international trade leads to uneven development and a continuously and indefinitely increasing gap between rich and poor countries because of international trade reflects the claims made by uneven development theories. Thus, another twentieth-century mode of thought was imposed on Smith's theory. Consequently, some started to depict Smith as a forerunner of uneven development theories (e.g., Rassekh 1998, p. 93). Since development economics leads an existence mainly on the fringe of economics, it is not surprising that the uneven development interpretation is the least widespread.

Misreading the Pattern of Trade in the Wealth of Nations

Jacob Viner once stated that "[t]races of every conceivable sort of doctrine are to be found in that most catholic book, and an economist must have peculiar theories indeed who cannot quote from the *Wealth of Nations* to support his special purposes" (1927, p. 207). However, this does not vindicate interpreting Smith's theory by the use of some scattered quotations taken out of context, which is what all three interpretations do to justify and reinforce their misinterpretations.

All three interpretations rely mostly on some paragraphs of Book IV of the *Wealth of Nations*—the neoclassical interpretation does so invariably. Here, Smith criticizes mercantilist as well as physiocratic ideas and policies based on his theory of capital accumulation and the natural progress of opulence developed in Books II and III. He does not introduce a theory of foreign trade in Book IV as is often claimed. Books II and III, in contrast, are mostly disregarded by all three interpretations—a neglect that has a long tradition (Tribe 2006). Yet, in these two books Smith describes in detail how capital accumulation is the driving force behind economic development and also behind foreign trade.[22]

The paragraphs most often used to prove the interpretation of a territorial division of labor in Smith's theory are *WN* IV.ii.11, 12, and 15. In *WN* IV.ii.15, Smith uses the example of grapes that could be produced in Scotland only at high cost. Scotland would be better off to use its resources in the production of some other commodities and to import wine. However, Smith does not establish a general rule of specialization here. He merely argues that "the natural advantages which one country has over another in producing particular commodities are *sometimes* so great" (emphasis added) that another country can only at excessively high cost produce such a good domestically. But as the word *sometimes* indicates, these are exceptional cases, which apply only to certain primary and agricultural

[22]On the relative neglect of capital accumulation in Smith's economic theory, see Schumacher (2018, pp. 13–14).

goods, as I have discussed above. In the main, a commodity will be produced both at home and abroad. He uses grapes as an evident and ridiculing example against "Restraints upon the Importation from foreign Countries of such Goods as can be produced at Home," which is the title of this chapter. Smith does not argue for specialization here but rather argues against monopolies that depress competition and divert capital to less productive employments. Concerning *WN* IV.ii.11-12, these paragraphs putatively demonstrate that specialization between countries is comparable to specialization between individuals. It is often argued that Smith's theory of foreign trade is merely an extension of the division of labor between individuals and thus ruled by the same principles. These two paragraphs, however, do not make such an assertion. Rather, Smith argues here that trade between individuals is always advantageous to those involved and the same is true for trade between countries, otherwise such a trade would not take place. Smith does not go any further with his comparison here. He does not argue that both individuals and countries will specialize analogously. The comparison between individuals and countries is taken out of context in order to justify an interpretation based on international specialization, which Smith himself does not do.[23] In Smith's theory, economic development leads to division of labor and thus to evermore specialized occupations. But this also means that economic development and a more extensive market allow for the emergence of new occupations, resulting in the production of new commodities and services (*WN* I.iii). While most workers will specialize completely and will "be confined to a few very simple operations; frequently to one or two" (*WN* V.i.f.50), a country as a whole will not specialize completely or even partially. Rather, its production diversifies. Or to put it differently, while the individual employment becomes more specialized, the overall production of a country becomes more various.

Proponents of the increasing returns interpretation and the uneven development interpretation refer, in addition, to the first chapters of Book I, in which Smith describes the (mechanical) division of labor. This is usually done for two reasons. First, the importance of increasing returns in Smith's theory should be demonstrated. To this end, an international territorial division of labor is wrongly read into these chapters. Second, further rules of international specialization should be derived from specialization between individuals. This is done by using Smith's example of "a philosopher and a common street porter," who were "very much alike" as children. Through different vocational education and work experience, these two developed into "the most dissimilar characters" (*WN* I.ii.4). It is argued that the same principle applies to countries.[24]

[23]There are further paragraphs in which Smith compares aspects of foreign trade with trade between individuals (e.g., *WN* II.v.20, IV.iii.c.9, and IV.iii.c.11). Those aspects include that trade "ought naturally to be, among nations, as among individuals, a bond of union and friendship" (*WN* IV.iii.c.9) and that it is easier to get wealthy if your neighbors are wealthy (*WN* IV.iii.c.11). These paragraphs do also not indicate that countries specialize comparable with individuals.

[24]See, e.g., Negishi (1985, p. 34; 1989, p. 95); Elmslie and James (1993, p. 66); Elmslie (1994, p. 267n); Milberg and Elmslie (1993, p. 54n); Buchanan and Yoon (2002, pp. 404–405); and Morales Meoqui (2014, p. 24). I myself have used this fallacious comparison (Schumacher 2012, p. 63). This misinterpretation might be the fault of the editors of the influential *Glasgow Edition of the Works and Correspondence of Adam Smith.* It includes a footnote at the end of *WN* IV.ii.15, in which Smith refers to viticulture in Scotland: "See above, I. ii.4." As far as I am aware, the philosopher–street porter example was applied to foreign trade only after the publication of the *Glasgow Edition* and might therefore be a direct result of it. Smith does indeed apply the "Smithian view of specialisation" mentioned in the introduction to individuals, echoing the sentiment that all men are created equal.

However, not only does Smith not mention foreign trade in this paragraph, but he also does not mention it at all in the whole chapter that contains this paragraph. In Smith's theory, countries will not specialize and become evermore different as individuals do. This conflation relies on a misreading of this paragraph of the *Wealth of Nations.* It is common in modern trade theory to draw a comparison between the specialization of countries and individuals. This is yet another example of how a modern way of thinking is erroneously imposed on Smith.

Proponents of the uneven development interpretation point also to paragraph *WN* I.i.4, in which Smith demonstrates that capital accumulation leads to an enhanced mechanical division of labor and illustrates this by comparing England, France, and Poland. It is here that Smith also notices that the division of labor can be enhanced further in manufacturing than in agriculture (*WN* I.i.4). Since wages increase with capital accumulation, Smith shows that unit costs in agriculture might even rise with economic development, while in manufacturing they will fall. Thus, Poland might be able to compete with richer England and France in agricultural, but not in manufactured, commodities. Proponents of the uneven development interpretation wrongly derive rules for an international specialization from this example. Smith does not derive such rules here. In this example, he elucidates the differences between rich and poor countries. He does not expound a theory of economic development, and neither does he claim that agricultural production is disadvantageous for a country. The opposite is true: agriculture is the basis for opulence![25]

Proponents of the uneven development interpretation lastly refer to the *Early Draft of Part of the Wealth of Nations* and the *Lectures on Jurisprudence.*[26] Parts of these writings indeed suggest that trade benefits rich countries more than poor countries. However, they should be referred to carefully. Smith was cautious about his publications. Close to his death he asked for all his manuscripts to be destroyed, except a few that he deemed publishable (Rae 1895, p. 434). The *Early Draft* escaped this destruction but was never intended by Smith for publication. The *Lectures on Jurisprudence* consist of student notes and were not written by Smith himself. Above all, these works entail Smith's early thoughts. They differ significantly from the *Wealth of Nations* in the treatment of economic development. Most important, the role of capital and its accumulation is absent in these early works. Smith introduces capital accumulation only in the *Wealth of Nations*, probably as a result of physiocratic influences, and makes it "the centrepiece of his theory of growth and development" (Prendergast 2010, p. 420).[27] Capital accumulation is, however, crucial to understand Smith's treatment of foreign trade in his *Wealth of Nations.*

[25]Some use this example to suggest that Smith came close to developing a theory of comparative advantage (e.g., Blecker 1997, p. 532; Bloomfield 1975, p. 457; Kibritçioglu 2002, p. 4; Rassekh 2015), implying that Smith in fact intended to do this. Others use the term "comparative advantage" in connection with Smith, partly based on this example (e.g., Morales Meoqui 2014, pp. 32–33; Negishi 2004; Tribe 2006). But such a misleading use suggests a connection between Smith and the static theory of comparative advantage as it is presented in today's textbooks. Additionally, the theory of comparative advantage rests on rigid assumptions (Schumacher 2013), which Smith did not share, and to attribute it to Smith is another way of imposing nineteenth- and twentieth-century modes of thoughts on Smith.

[26]The *Lectures* originated between 1762 and 1764; the *Early Draft* was written presumably earlier.

[27]On the differences between Smith's earlier works and his *Wealth of Nations*, see also Eltis (1988, 2004); McNally (1988, pp. 234–250); Meek (1954); Santos (1998).

IV. CONCLUDING REMARKS

"Adam Smith knew little or nothing about the nature of trade or commerce, and, being conscious that he could not explain what he did not understand, he very wisely said let trade be free." So wrote James Syme (1821, p. 349) in the early nineteenth century. Classical economists in the nineteenth century held Smith in higher esteem and were more enthusiastic about free trade than Syme. However, they too were often critical of Smith's theoretical treatment of foreign trade. One reason is that Smith, unlike them, did not understand international trade foremost in terms of a territorial division of labor. In contrast to classical economists, neoclassical economists valued Smith's trade theory higher, integrating it into a neoclassical Whig history of international trade theory, which tells a straight development starting with Smith's alleged *theory of absolute advantage* via the classical theory of comparative advantage to the modern neoclassical theory of comparative advantage (Schumacher 2012). Smith is portrayed as deserving some credit, since his theory is ultimately based on the right idea, the territorial division of labor. However, Smith's approach is depicted as deficient because he failed to develop a theory of comparative advantage, the high point of trade theory in this neoclassical historiography. In order to fit Smith into this neoclassical Whig history, his theory had to be completely disfigured.[28] In the late twentieth century, the increasing returns interpretation and the uneven development interpretation increased the image of Smith as a trade theorist once more. They both portray him as an inspiring trade theorist whose important insights have been neglected by mainstream economics for a long time due to the narrowness of neoclassical theory.

Despite their differences, all three interpretations are based on the erroneous attribution of international specialization to Smith's trade theory. This misinterpretation is justified by a selective reading of Smith's writings and above all by imposing modern modes of thought on Smith's theory. The neoclassical interpretation is an example of what Donald Winch describes as "the application of what are basically nineteenth-century perspectives to what is quintessentially a work of the eighteenth century," which "not only introduces various artificialities and anachronisms, but obscures important features of Smith's project" (1978, p. 165). Within the scope of this article, these nineteenth-century perspectives are, above all, the conception of international trade purely in terms of a territorial division of labor. Additionally, a static framework based on the most efficient use of existing resources was imposed on Smith's theory in retrospect, as were the conception of foreign trade as an independent phenomenon and the identification of international specialization with specialization between individuals. The increasing returns interpretation and the uneven development interpretation apply additional twentieth-century perspectives of international trade theory to Smith's approach, adding new dimensions to obscuring Smith's original theory. By proposing these interpretations, one constructs, as Winch aptly described it, "a mirror in which we see our own reflection" (1978, p. 184). Each interpreter sees only their own theoretical approach in Smith's writings. To this end, Smith's theory had to be distorted or even adulterated and his original ideas were lost.

[28]There has been some discussion about the legitimacy of Whig history in historiography. I do not want to contribute to this broader debate here. For a discussion among historians of economics, see, e.g., Samuelson (1987); Schabas (1992); Weintraub (2016).

The discussion above shows that each interpretation of Smith's trade theory emerged only after the related theory—neoclassical trade theory, new trade theory, uneven development theories—had been established and consolidated. By this time, their ideas had spread and the proponents of each theory started reading Smith through their own spectacles. Additionally, they started writing their own respective history. They decided who they wanted to be aligned to. In all three cases, Smith's inclusion was an afterthought. His theory did not inspire any of the three theories. A question I have not raised so far is why three completely different traditions in international trade theory would try to project their own theories on Smith and align their theories with his name. The reasons are above all legitimacy and custom (Schumacher 2012, pp. 72–73). Smith is widely adored as one of the leading lights of the Scottish Enlightenment—not only in economics but in social sciences as a whole. Referring to Smith as a forerunner promises to boost the standing of one's own theory. It is thus put in relation to the authoritative and prestigious name of Adam Smith. Invoking that a theory or concept follows the footsteps of Smith legitimizes it and increases its reputation. While classical economists had to distinguish themselves from Smith to stress the new aspects of their own theories, neoclassical historiography incorporated the *father of economics.* Aspiring theories also try to increase their image and legitimacy by invoking Smith as their forerunner. Especially by arguing that they—and not the incumbent, neoclassical theory—are the real successor of the father of economics, they tried to increase their own standing. Apart from the legitimacy, custom also plays a role. Once an interpretation of Smith's theory is established, it will be adopted by others who have never read Smith's work completely or not even partially —after all, the *Wealth of Nations* is a lengthy book. In this way, a misinterpretation spreads.

It is true, as Keith Tribe notes, "that Smith's own arguments have for so long been pulled apart and reassembled for other purposes, passages being cited without regard for their place in the work as a whole, that any direct contact with Smith's own line of reasoning has long disappeared from the literature" (2006, p. 61). In this article, I have tried to show how this was done in respect to the pattern of trade in Smith's theory. Smith's trade theory differs from all three modern interpretations. Smith neither assumed an international territorial division of labor nor set up a foreign trade theory separate from his overall theory of economic development. Rather, foreign trade is embedded in his overall theory of domestic economic progress based on capital accumulation. Foreign trade, in Smith's theory, is the result, not the cause, of opulence. In addition to capital accumulation, transport costs and preferences of capital owners also play a major role for international trade patterns. According to Smith's theory, international trade will predominantly take place between opulent developed countries, whereby traded commodities are mainly more sophisticated manufactured goods. Most commodities will be produced in most countries, increasing competition, which is highly beneficial for societies, according to Smith. Countries will diversify their production and become jacks of all trades in the course of their economic development.

To economists who are used to modern theories of international trade based on nineteenth- and twentieth-century perspectives—above all, an international territorial division of labor—Smith's trade theory might seem rather peculiar. It is, therefore, unsurprising that the few scholars who rightly notice that Smith does not base his trade theory on a territorial division of labor conceive this as a shortcoming of Smith (Rashid 1998, p. 24; Rothbard 1995, p. 442; Spengler 1959, pp. 400–401)—as did classical economists in the nineteenth century. However, this judgment might be unfair. I have abstained from evaluating Smith's trade, but two points should be mentioned at the end. First, the gravity model of trade, which is "one of the most successful empirical models in economics" (Anderson 2011, p. 134), concludes similar to Smith that the greatest share of trade will take place between the most developed and thus similar countries. Second, Jean Imbs and Roman Wacziarg have shown empirically that "countries diversify over most of their development" (2003, p. 64)—not specialize. This is also predicted by Smith's theory. According to Imbs and Wacziarg's study, this trend reverses only once a country has reached a very high standard of living. Smith does not predict such a reversal, but he was writing at a time when this high standard of living was far off. Thus, a genuine study of Smith's insights and economic ideas might still be relevant today, if they are correctly understood in the context of his time.

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