

Third Part:
The Laws of Distribution

Chapter 10
**The Necessary Relation
of the Laws of Distribution**

OUR PRECEDING EXAMINATION has shown that the current explanation for the persistence of poverty despite increasing wealth is no explanation at all. But by demolishing it, we have made the facts appear even more inexplicable. We have, in short, proved that wages should be highest where they are actually lowest.

At least we have discovered where it is useless to look. The cause of poverty is not lack of capital. Nor is it the limitation of nature. In short, it is not found in laws governing the production of wealth. Therefore, we must examine the laws governing its distribution.

First, let's outline the distribution of wealth. Since land, labor, and capital join to produce wealth, the output must then be divided among these three. To discover the cause of poverty, we will have to find the law that determines what part is distributed to labor (wages). Then to make sure this law is correct, we must also find the laws fixing what part goes to capital (interest) and what

part to landowners (rent).

Producing is not simply making things—it also includes increasing their value by transporting or exchanging them. Wealth is produced by the commercial community, just as it is by the agricultural or manufacturing community. In each case, some of it will go to the owners of capital, some to laborers, and some to the owners of land.

Additionally, since capital is constantly consumed and constantly replaced, a portion of the wealth produced goes toward the replacement of capital. It is not necessary to take this replacement of capital into account, however. It is eliminated by considering capital as continuous. We habitually do this, both in speaking and thinking of it.

The produce of the community is the general fund that supports all consumption. The term refers to wealth produced beyond what is required to replace any capital consumed in the process. Therefore, interest means what goes to capital after its replacement or maintenance.

Furthermore, some of the wealth produced is taken by government in taxes (except in the most primitive communities). Again, for our purposes in determining the laws of distribution, we may consider taxation either as not existing or as reducing output by that amount. Certain forms of monopoly exercise powers analogous to taxation, and may be treated likewise. (We will discuss these in Chapter 13.) After we have discovered the laws of distribution, we can then see what effect taxation has upon the process.

Economists do not understand these laws correctly, as we may see in any standard text. In all these works, we are told that the three factors of production are land, labor, and capital, and that the entire output is distributed to

their corresponding parts. Therefore, three terms are needed. Each should clearly express one part to the exclusion of the others.

Rent is defined clearly enough as the part that goes to owners of land. The term wages is also defined clearly enough as the part that is the return to labor. The third term, then, should express the return for the use of capital.

But here, we find a problem. In standard economics books, there is a puzzling ambiguity and confusion. The term that comes closest to exclusively expressing the idea of return to capital is interest. Interest implies the return for the use of capital, exclusive of any labor in its use or management, and also exclusive of risk.

Note that the word profits simply means what is received in excess of what is expended. Such receipts may include rent and interest and wages, including compensation for risk.* Therefore, profits cannot be used to signify the share going to capital—as distinct from that going to labor and to landowners. The term has no place in discussing the distribution of wealth between the three factors of production, unless extreme violence is done to its meaning.

To speak of the distribution of wealth into “rent, wages, and profits” is like dividing mankind into “men, women, and human beings.” Yet, to the utter bewilderment of the reader, this is what is done in all standard works. Undoubtedly, thousands have vainly puzzled over this confusion of terms, and abandoned their efforts in despair. Believing the fault could not be in such great thinkers, they assumed

* Today, some attribute risk-taking to a distinct factor, called “entrepreneurism”. George defined labor as all human exertion in production, whether mental or physical.

it must be their own stupidity. Reading John Stuart Mill, you can see this confusion exemplified by the most logical of English economists—in a manner more striking than I care to characterize.

No text, to my knowledge, brings these laws together so the reader can recognize their relation to each other. Instead, each is enveloped in a mass of reflections and dissertations. The reason is not far to seek: Bringing together the three laws of distribution, as they are now taught, shows at a glance that they lack necessary relation.

The laws of distribution are obviously laws of proportion. They must relate to each other so that given any two, the third may be inferred. To say that one part of the whole is increased is to say that one or both of the other parts must be decreased (or vice versa).

Say Tom, Dick, and Harry are business partners. The agreement setting the share of one also sets the shares of the other two, either jointly or separately. If Tom gets thirty percent, that leaves seventy percent to be divided between Dick and Harry. If Tom gets thirty percent and Harry fifty percent, that fixes Dick's share at twenty percent.

But in standard economic texts, there is no such relation among the laws of distribution of wealth. If we fish these laws out and bring them together, we find them stated as follows:

Wages are determined by the ratio between capital available for labor and the number seeking employment.

Rent is determined by the margin of production. That is, rent equals the amount of produce in excess of what could be produced from the poorest land in use with the same amount of labor and capital.

Interest is determined by the demands of borrowers

and the supply of capital from lenders.

Or, if we take what is given as the law of profits, it is determined by wages, falling as wages rise and rising as wages fall. (What Mill calls "the cost of labor to the capitalist.")

Bringing these together, we immediately see a problem: They lack relation to each other, which the true laws of distribution must have. Since they do not correlate, at least two of the three must be wrong.

We must then seek the true laws of distribution that divide what is produced into wages, rent, and interest. The proof that we have found them will be in their correlation.

To recapitulate what we have discovered in our investigation:

Land, labor, and capital are the factors of production. Land includes all natural opportunities or forces. Labor includes all human exertion. Capital includes all wealth used to produce more wealth.

The output is distributed in returns to these three factors. Rent is that part that goes to owners of land as payment for the use of natural opportunities. Wages are that part that constitutes the reward for human exertion. Interest is that part that constitutes the return for the use of capital.

These terms mutually exclude each other. The income of any individual may be made up from any one, two, or all three of these sources. But to discover the laws of distribution we must keep them separate.

I think the error of political economy has now been abundantly revealed, and can be traced to an erroneous viewpoint.

We live in a society where capitalists generally rent land and hire labor. They thus seem to be the initiators or first movers in production. Living and making observations in

this state, the great developers of economic science were led to look on capital as the prime factor in production. They saw land as its instrument, and labor as its agent or tool. This is apparent on every page. It is in the form and course of their reasoning, in the character of their illustrations, and even in their choice of terms. Everywhere capital is the starting point, and the capitalist the central figure.

This goes so far that both Smith and Ricardo use the term "natural wages" to express the minimum on which laborers can live.

On the contrary, unless injustice is natural, everything a laborer produces should be his natural wages. This habit of looking on capital as the employer of labor began when Adam Smith, in his first book, left the viewpoint that "the produce of labor constitutes the natural recompense or wages of labor." Instead, he adopted the view in which capital is considered as employing labor and paying wages.

But when we consider the origin and natural sequence of things, we see that this reverses the natural order of things. Capital does not come first, it comes last. Capital is not the employer of labor—it is, in reality, employed by labor.

The matter that labor converts into wealth comes only from land. There must be land before labor can be exerted. And labor must be exerted before capital can be produced. Capital is a result of labor, a form of labor, a subdivision of the general term. It is only stored-up labor, used by labor to assist it in further production. Labor is the active and initial force. Therefore, labor is the employer of capital, not vice versa—and it is even possible for labor to produce wealth without being aided by capital.

So the natural order is this: land, labor, capital.

Instead of using capital as our initial point, we should start from land.

