

Chapter 15

The Law Of Wages

THERE IS no common rate of wages in the same sense as the common rate of interest, which is relatively specific at any given time and place. Wages vary with individual abilities. As society becomes more complex, there are also large variations among occupations. Nevertheless, there is a certain general relation between all wages. This concept—that wages are higher or lower at one time or place than another—is quite clear. So wages must rise and fall according to some law.

There is a law as basic to political economy as the law of gravity is to physics. The fundamental principle of human action is this:

People seek to gratify their desires with the least exertion.

Clearly, this principle will tend, through competition, to balance rewards for equal exertion under similar circumstances. When people work for themselves, this operates largely through price fluctuations. The same tendency governs relationships between those who work for themselves and those who work for others. Given free conditions, no one would work for someone else if they could make the same amount working for themselves.

But output does not depend only on the intensity or quality of labor. Wealth is the product of two factors—land and labor. A given amount of labor yields various re-

sults, depending on the powers of the natural opportunities to which it is applied. This is easily seen in fundamental occupations, which still form the base of production—even in the most highly developed societies.

People will not work at a lower point while a higher one is available. So, the highest point of natural productiveness available will be same as the lowest point at which production continues. This is called the margin of production.

Wages will be set by the output at the most productive point open to labor. They will rise or fall as this point rises or falls.

To illustrate, consider a simple society in which each person is self-employed. Let's say some hunt, some fish, some farm. At first, all land being used yields a similar return for similar effort. Allowing for differences of ease, risk, and so on, wages will be approximately equal in each. That is, equal exertions will yield equal results for hunting, fishing, or farming. Wages will be the total production of labor. (Remember, even though there are no employers yet, there are still wages—that is, the return for labor. But no one would work for someone else, at this stage, unless they received the full, average results of labor.)

Time passes. Cultivation now occurs on land of different quality. Wages will no longer be as before—the full, average production of labor. Instead, wages will be the average at the margin of production—the point of lowest return. Since people seek to satisfy their desires with the least exertion, this point will yield a return to labor equivalent to the average return in hunting and fishing.

This equalization in return will be brought about by prices. Labor no longer yields equal returns for equal exertion. Those working superior land get greater results,

for the same exertion, than those on inferior land. Wages, however, are still equal. The excess received from superior land is, in reality, properly called rent. If land has been subjected to individual ownership, this is what gives it value.

Circumstances have changed. To hire others, an employer need pay only what the labor yields at the lowest point of cultivation. If the margin of production sinks lower, wages will also drop. If it should rise, wages must also rise.

We have deduced the law of wages from an obvious and universal principle—that people will seek to satisfy their wants with the least exertion. Wages depend on the margin of production. They will be greater or less depending on what labor can get from the best natural opportunities available to it.

We deduced this from simple states. If we examine the complex phenomena of highly civilized societies, the same law applies. Wages differ widely in these societies, but they still bear a fairly definite and obvious relationship to each other.

Of course, this relation is not invariable. A well-known entertainer may earn many times the wages of the best mechanic, yet at some other time the same entertainer may barely command the pay of a footman. Some jobs pay high wages in big cities, while in a small town the pay is low. We need not dwell on what causes wages to vary among different jobs. This has been admirably explained by Adam Smith and the economists who followed him.* They have

* Adam Smith has summarized these circumstances. They include: the difficulty of the job itself; the difficulty and expense of training; the constancy of employment; the degree of responsibility; and the probability of success. The last is analogous to the element of risk in profits. It accounts for the high wages of successful doctors, lawyers, actors, etc.

worked out the details quite well—even if they failed to comprehend the main law.

It is perfectly correct to say that wages of different occupations vary according to supply and demand. Demand means the request that the community makes for particular services. Supply is the relative amount of labor available to perform those particular services.

However, when we hear (as we often do) that the general rate of wages is determined by supply and demand, those words are meaningless. For supply and demand can only be relative terms. Demand for labor can only mean that some product of labor is offered in exchange for (other) labor. Likewise, the supply of labor can only mean labor offered in exchange for the products of labor.

Thus, supply is demand, and demand is supply. In the whole community, they must be coextensive with each other. Wages can never permanently exceed the production of labor.

The high wages of some occupations resemble lottery prizes, where the great gain of one is taken from the losses of many others. This accounts for the high wages of successful doctors, lawyers, actors, and the like. It is also largely true of wages of superintendence in mercantile pursuits, for over ninety percent of such firms ultimately fail.

Greater abilities or skill, whether natural or acquired, command (on average) greater wages. These qualities are essentially analogous to differences in strength or quickness in manual labor. Higher wages, paid to those who can do more, are based on the wages of those who can only do an average amount. So wages in occupations requiring superior abilities must depend on common wages paid for ordinary abilities. In these occupations, the de-

mand is more uniform and there is the greatest freedom to engage in them.

These gradations of wages shade into each other by imperceptible degrees. In each occupation, there are those who combine it with others, or alternate between fields. All mechanics could work as laborers, and many laborers could easily become mechanics. Mechanics generally earn more than laborers. Still, there are always some mechanics who do not make as much as some laborers. The best paid lawyers receive much higher wages than the best paid clerks. Yet, the best paid clerks make more than some lawyers. In fact, the worst paid clerks make more than the worst paid lawyers. Meanwhile, young people coming into the ranks are drawn to the strongest incentive and least obstruction.

Thus, the differences between occupations are so finely balanced that the slightest change is enough to guide their labor in one direction or another. Experience shows that this equilibrium will be maintained even in the face of artificial barriers. They may interfere with this interaction, but they cannot prevent it. They operate only as dams, which pile up the water of a stream above its natural level, but cannot prevent its overflow.

Thus, it is evident that wages in all strata must ultimately depend upon wages in the lowest and widest stratum. The general rate of wages will rise or fall as the lowest wages rise or fall. The primary and fundamental occupations, on which all the others are built, are those that obtain wealth directly from nature. Hence the law of wages applying to those occupations must be the general law of wages. And wages in such occupations clearly depend upon what labor can produce at the lowest point of natural pro-

ductiveness to which it is regularly applied. Therefore:

Wages depend upon the margin of production. That is, wages depend on the yield labor can obtain at the highest point of natural productiveness open to it without the payment of rent.

Our demonstration is complete. The law just obtained is identical to the one we deduced as a corollary of the law of rent. It also harmonizes completely with the law of interest. It conforms with universal facts, and explains phenomena that seem unrelated and contradictory without it.

Specifically, it explains these four conditions: Where land is free and labor works without capital, the entire output will go to labor as wages. Where land is free and labor is assisted by capital, wages will consist of the whole produce less what is necessary to induce the storing up of labor as capital. Where land is subject to ownership and rent arises, wages will be fixed by what labor could secure from the highest natural opportunities open to it without paying rent (i.e., the margin of production). Where all natural opportunities are monopolized, wages may be forced by competition among laborers to the minimum at which they will consent to reproduce. Clearly, the margin cannot fall below the point of survival.

To recap: The law of wages is a corollary of Ricardo's law of rent. Like it, the law of wages contains its own proof, and is self-evident as soon as it is stated. It is only the application of the central truth that is the foundation of economic reasoning—namely, that people seek to satisfy their desires with the least exertion. All things considered, the average person will not work for an employer for less than can be earned in self-employment. Neither will a person choose self-employment for less than could be

earned working for an employer. Hence, the return labor can get from free natural opportunities must set the wages for labor in general. Said another way, the line of rent is the necessary measure of the line of wages.

In fact, recognizing the law of rent depends upon accepting (often unconsciously) the law of wages. What makes it clear that land of a particular quality will yield rent equal to its surplus over the least productive land in use? Because we know that owners of better land can get others to work for them by paying what workers can get on poorer land.

The law of wages is so obvious that it is often understood without being recognized. People who do not trouble themselves about political economy grasp it in its simpler forms, just as those unconcerned with the laws of gravitation know that a heavy body falls to the earth. It does not require a philosopher to see that the general rate of wages would rise if natural opportunities were available where workers could earn more than the lowest wages. Even the most ignorant placer miners of early California knew that as these mines gave out or were monopolized, wages would fall.

It requires no finespun theory to explain why wages are so high relative to production in new countries where land is not yet monopolized. The cause is on the surface. No one will work for another for less than can be earned through self-employment—such as going nearby and independently operating a farm. It is only as land becomes monopolized, and these natural opportunities are shut off, that laborers are forced to compete with each other for work. It then becomes possible for a farmer to hire hands to do the work—while the farmer lives on the difference

between what their labor produces and their wages.

Adam Smith himself saw the cause of high wages where land was still open to settlement. Unfortunately, he failed to appreciate the importance and the connection of the fact. In the *Causes of the Prosperity of New Colonies*, he reports:

*Every colonist gets more land than he can possibly cultivate. He has no rent and scarce any taxes to pay. He is eager, therefore, to collect laborers from every quarter and to pay them the most liberal wages. But these liberal wages, joined to the plenty and cheapness of land, soon make these laborers leave him in order to become landlords themselves, and to reward with equal liberality other laborers who soon leave them for the same reason they left their first masters.**

It is impossible to read the works of Adam Smith and other economists without seeing how, over and over again, they stumble over the law of wages without recognizing it. If it were a dog, it would bite them! Indeed, it is difficult to resist the notion that some of them actually saw it, but were afraid of its logical conclusions. To an age that has rejected it, a great truth is not a word of peace, but a sword!

Before closing this chapter, let me remind the reader that I am not using the word wages in the sense of a quantity, but in that of a proportion. When I say that wages fall as rent rises, I do not mean that the quantity of wealth laborers receive as wages is necessarily less. I mean that the proportion it bears to the entire output is less. The

* Chap. VII, Book IV, *Wealth of Nations*.

proportion may diminish while the quantity remains the same, or even increases.

For example, suppose the margin of production declines. (We will say from 25 to 20.) As rents increase by this difference, the proportion given in wages must decrease to the same extent. In the meantime, the productive power of labor has increased. Technology may have advanced, or increasing population may make possible greater economies of scale. The same effort at point 20 now produces as much wealth as point 25 used to. The *quantity* of wages remains the same, though the *proportion* has decreased.

This relative fall of wages will not be noticed in the comforts of the laborers. It will be seen only in the increased value of land—and in the greater income and extravagance of the rent-receiving class.