THE THIRD FACTOR OF PRODUCTION.

WEALTH.—By wealth is understood all those material utilities which Labour has produced or collected, and which minister to man's maintenance or enjoyment.

Economists (having the processes of exchange in view) have restricted the term to goods having an exchange value. But this arbitrary restriction injuriously limits the field of inquiry, shutting us off from many aspects of the subject which it is desirable for us to examine, and often leading us absolutely astray. The house, clothes, tools, live stock, and other accumulations of Robinson Crusoe constituted his wealth in the sense in which everyone in daily life understands the word; none the less that there being no one with whom he could exchange they had no exchange value. Similarly the macadamised highways, the bridges, docks, and public buildings of the State are as much a part of the wealth of the country, that is, have the same origin and fulfil the same purpose, as the railways, factories, and mansions in private hands; none the less that they have no exchange value, seeing that the State has no idea of disposing of them, and could hardly find a purchaser for some of them if it had.

What the world wants to know is the laws that govern the production and distribution of *utilities*; of the things that minister to our comfort and enjoyment, no matter whether they have an exchange value or not. Where they have (as they generally have), a special field of inquiry (the field of exchange) is opened up; but the whole inquiry ought not to be limited to one particular part. However, the point will not much concern us, so we need not dwell upon it.

All wealth, whether we take it in its ordinary and broad sense or in its technical and restricted sense, is produced by human effort (usually called *Labour*) acting on the raw materials and forces of the earth, briefly expressed by the term *Land*, because they are all parts or properties or adjuncts of the land; the minerals that lie under the surface, the waters that flow over it, the fertility, accessibility, aspect, rainfall of any given piece of land being the elements or attributes that give that land its utility, just as the intelligence, knowledge, strength, activity of a labourer are the properties that alone make his labour worth having. Indeed, if you take away the attributes of anything from the thing itself, there is hardly anything left, for we know nothing of anything but by its attributes. Moreover, land itself, or the crust of the earth, is the most important, from the productive point of view, of all the gifts of nature, and the term Land conveniently covers them all; and every spontaneous product of the earth before labour has touched it, the trees of the forest, the fish of the sea, everything, in short, which is the pure and unassisted product of nature is included in the same term. I do not invent this comprehensive term. I take it from the Economists as I find it; but if anyone objects to it, he can substitute the term nature.

LABOUR.—By labour is understood human effort of every kind, mental or bodily, applied to useful purpose; to work, as distinguished from play; that is, to the production of some utility or to the acquisition (not indulgence) of some enjoyment.

The industry, skill, knowledge, judgment of the labourer, being reckoned as properties of his labour, are included in the term labourer, just as the fertility and so on of the land are included in the term land.

Land and labour thus broadly understood as nature and man's action upon it are the matter and force of industry, the two prime factors of production.

Instruments.—But man with his naked fingers could hardly satisfy a single want, certainly make no progress, no matter how favourable his surroundings. The savage could kill no game without a weapon of some kind which we may call his tool of trade; could not till the ground without a hoe, could not construct a dwelling without a stone axe or instrument of some sort; and with every step forward in improvement of his condition and development of his nature the number and complexity of his tools and appliances and the necessity for them will increase. The first act of labour then in every case will be to procure a tool. So indispensable to progress and even to existence are tools that they have been fairly called the third factor of production; though they are so only in a derivative sense, being themselves the product of labour acting on the materials and forces of the earth—that is, upon land.

The term Tools, however, is hardly comprehensive enough for our purpose, custom having restricted it to the simpler sort of appliances. We want a term that shall cover all appliances; that shall express the most complicated machine as well as the simplest tool, and that shall include those raw materials, themselves the product of labour, that labour works *on* as well as the tool it works *with*; that shall include the cloth for the coat as well as the needle, the plank as well as the hammer and nails; for these raw products of our industry, which we work up, are as much the instruments of production as the tools we work them up with; one is as necessary as the other, and each is useful only as a means of producing something else. The term Instruments, then, is comprehensive enough to cover both, familiar enough to be in no danger of being misunderstood, and has not been appropriated for any technical purpose, so we shall adopt that term. Instruments, then, represent the third factor of production.

All the accumulated products which constitute wealth may be classified under two heads: products which minister directly to maintenance or enjoyment, as a loaf, a coat, a necklace, requiring no further labour to fit them for such use, and which, therefore, we shall call final products; and products whose function is not to minister directly to maintenance or enjoyment, but only as a tool with which, a material out of which, or a vehicle by means of which, we can procure the things that do, and which, therefore, we call instruments; as a spade, a roll of cloth, a cart. No doubt there are many articles which we might feel doubtful whether to classify as instruments or final products, and others again which may be changed at will from one category to the other, as when a carriage horse, bred and kept solely for enjoyments and therefore figuring as a final product, is set to draw a plough and so becomes an instrument. But these niceties do not affect the argument. What we want is not to make a classified catalogue of goods, but to clear our ideas; and all we are now concerned with is this, that all wealth consists of two classes of goods only—goods which represent the crown of labour and are fitted directly for enjoyments, which, therefore, we call final products, and goods whose use is only to produce other goods, and which, therefore we call instruments.

Any given article comes at any given moment under one or other of these two heads, no matter whether we feel sure under which head to place it, or whether we may find reason to change it from one category to the other.

The productive power of a community depends (*ceteris* *paribus*) on the number and efficiency of the articles which it can use as instruments for the work it wants to do.

So far, I think, there is nothing new, nothing on which economists are not already pretty well agreed; and when they expressed this third factor of production by the term Capital, there can be little doubt that by capital they originally meant instruments, and nothing else.

And the word Capital would have done as well as any other for the purpose but for the fact—the fatal fact—that the usage of the world had already appropriated it to mean something that at first sight seems much the same thing, but which, as we shall see, is radically different, and in some aspects even absolutely opposed to it.

Ask a business man what he understands by Capital, and he will reply by an illustration; he will say that £1,000 is Capital.

He does not care what the £1,000 consists of. It may consist of coin, or of bank-notes, or of a mere entry to credit at a bank, or of goods, or mining scrip, or shares in a company, or debts due by solvent people, or of title deeds authorising him to exact rent from land, or Government debentures entitling him to draw on the general revenue. Whatever it is, so long as it can command £1,000 in cash, or goods, or services, it is to him £1,000, and £1,000 is Capital.

He knows, in short, exactly what he means by it, and he means *money*. Not money in the narrow and technical sense of coin of the realm, but *money power*, that general command of the market or purchasing power, of which coin is merely the outward and visible symbol and token of exchange.

To be recognised as a man of money, and to exercise money-power, a man need not have a sovereign, or a bale of goods in his possession. In the vast majority of cases his money consists in a mere claim; a claim on a bank, on a mine, on an estate, on the general revenue, on a private debtor. Indeed, when we look closely into it, it is *always* a claim.

Even when it consists of actual coin, that coin is only a metal ticket representing so much purchasing power free of further labour; just as a bank-note is a paper one, indicating that its possessor has rendered some service, real or imaginary, entitling him to draw to that amount on the general stock. Money, in short, in its broad, every-day commercial sense, represents (no matter what form it may assume) the power to secure services to a given extent, without rendering any service in return, by simply transferring the token (coin or note) when it is a token, or exhibiting the authority (title deed or debenture) when it is an authority.

Whosoever prospers in business does not convert his gains into coin to be hoarded, or into goods to be stored up, but into claims to be registered. A is owed something by B, C, and D. B pays him in currency (coin or notes), and A, by transferring these tokens, can get goods from anybody. C pays him by a cheque, which merely means that C had a previous claim on a bank, and now transfers that claim to A. D does not pay him at all, but gives an acknowledgment of indebtedness, and A keeps his claim hanging over him.

The claim in any given case may be morally good or bad. It may represent real services actually rendered, or it may represent impudent blackmail, or corrupt grant on the public treasury; but good or bad, so long as the law recognises it as a claim, the public recognises it as money; that is, as money-power, as that which constitutes the possessor a monied man.

But claims are not the third factor of production. They might all be obliterated by legal fiat; and though great injustice might be done, and the whole industrial system put out of joint for the moment, the working, productive power of the Community would not be impaired a whit.

The efforts that D makes, the land he works on, the materials he works up, the tools he works with, are none of them more effective because A has a claim on the result. However justifiable it may be, however desirable in the public interest that it should be recognised, the claim, as a claim, adds nothing to the sum of enjoyment or production.

Whence we perceive that the greater part of what is called "Accumulated Capital" represents no accumulation at all; or (to put it differently) represents not accumulated goods but accumulated debts. For a claim and a debt are the same thing viewed from opposite sides.

A having by service rendered, or in some way or other become entitled to demand cash or goods from B, waives payment for the time being, and allows B (or someone else, C, to whom the debt is transferred) to consume the goods instead of receiving and consuming them himself; B and C having to provide such goods hereafter out of the future produce of his labour.

You may say that this amounts practically to an accumulation, because B, being relieved of payment of the goods, will employ them productively and produce them. But that is not certain. What is certain is that the goods are not really accumulated, but consumed just as much as if payment had been made, only they are consumed by B instead of by A, and what remains is a claim.

When to this accumulation of liabilities (figuring as "savings of capital") is added interest, we shall see that so far from assisting industry, it weighs upon it. Indeed it may happen, and very often does happen, that this waiving of present payment injures the debtor in the end much more than it relieves him in the present. The debt, light at first, accumulates till the weight becomes crushing; when one of two things happens: either the debtor is ruined by payment, or he goes bankrupt, and the whole "accumulation" disappears.

However I am not arguing that credit is a bad thing, but only illustrating my point that a great part of the so-called accumulations of Capital are wholly imaginary; that is, that they are not accumulations of goods but of debts.

So far as to the business man's idea of Capital: he knows exactly what he means by it, and he means Money. But if you ask the Economist what he means by it, you get no such prompt and definite reply. You find, on the contrary, that no two economists mean the same thing; and further (if you look closely), you will find that no single economist ever keeps strictly to his own definition.

You will find, too, that these differences are not merely as to the best way of expressing the thing, but as to the very nature of the thing itself. Mill calls it—The fund for carrying on present production; Bonamy Price—Wealth employed to produce wealth; Senior—Whatever gives a profit; Perry says—It is either a commodity or a claim, but not personal powers; George calls it—Wealth in course of exchange; Giffen includes all accumulations under it, making no distinction between capital and other forms of wealth; Huxley includes under it the muscular force of the labourer, the food he eats, the grass of the field, anything and everything, in short, by aid of which man lives and works.

I was once at a dinner of the Political Economy Club in London, whereat was distributed a printed list of subjects for discussion, amongst which was, "What is Capital?"

Imagine a meeting of leading Mathematicians meeting to discuss "What is a right line?"

I suppose that if non-mathematicians heard of such a debate, they would conclude that if mathematicians were not yet agreed as to what a right line was, mathematics could hardly be worth studying. For a clear idea of a right line is not more necessary to mathematics than is to political economy a clear idea of capital, or, at any rate, of that third factor of production which economists profess to express by the term capital.

There seems no doubt that the economists meant at starting to signify by capital—*Instruments;* the tools, appliances, and materials with which man supplemented his naked fingers in the act of production, and without which his naked fingers would have helped him but little. They meant instruments as instruments, and not money; that is, if they included money it was only in a secondary sense, as that with which one could procure instruments. While the man of business, on the contrary, understands by it money as money and not instruments; that is, if he includes instruments it is only in a secondary sense, as that which one can sell for money, or by aid of which one can make money; money being that with which one can purchase the labour of others, or procure goods *already in existence;* while instruments are that by aid of which labour (one's own or another's) is made more efficient, and fresh goods are *brought into existence.*

The two ideas are not only different but directly opposed to each other, and are perpetually in conflict—a conflict which could have but one result. For as the clear and definite idea (that of the man of business) overpowers the obscure and variable (that of the contending economists); as the sense of the many in the market and the street overpowers the sense of the few in the closet, so in public life;—in the press, on the platform, the leaders of the public, addressing the public on public affairs, use the word (capital) in the sense in which the public understands the word, and the public understands it as money.

Moreover, the economist is himself a man of the world and a citizen before he is an economist, and as such uses the word, *must* use it continually in the common sense, till the distinction between the two becomes lost, or is remembered only to be forgotten the next minute; until again half conscious of his floundering, he tries to express himself so as to cover both meanings, to reconcile the irreconcilable. What confusion and error have arisen from this we shall see as we proceed. The whole difficulty has arisen from undertaking to say that A shall mean B; that a word which universal custom has decreed shall mean money as money and not instruments, shall mean instruments as instruments and not money.

When Mill described the third factor of production as wealth devoted to productive purposes, he came very near the correct definition. Very near, but he just missed it and passed by. For, starting from the assumption that wealth is that only which has exchange value, and placing the distinction between capital and not capital in the mind of the capitalist and not in the nature of the article, and saying that anything which can be exchanged for other things is capable of contributing to production in the same degree as those other things, he clearly lost sight for the moment of the difference, the enormous difference, between production and profit-making; between absolute gain and relative gain; between the effect on the sum total of goods and enjoyments and the effect on the capitalist's pocket. He uses the word capital, as the business man avowedly does, to represent simply that with which a man proposes to enrich *himself*, not that by which wealth in the mass is to be increased.

Profit is no test of productiveness. It constantly happens that profit is made without adding anything to the sum total of goods and enjoyments; often by actually diminishing it. There are rings and monopolies of all kinds that make their profit by restricting output and so forcing up price. There are makers of gold trowels for laying foundation stones and other useless articles representing high value, and undertakers who use up useful timber and metal in funereal frippery to be straightway buried under ground, and countless others of the same type who make their profit by sheer waste of good materials. A hundred-guinea ball dress that will be used perhaps twice, and then discarded, represents rather a waste of a hundred guineas than a production of it. On the other hand, there are businesses that bring no profit to the promoters, but yet are highly productive, though, unfortunately, the promoters do not often continue them long. The gentleman farmer, for example, who loses two or three hundred a year by what is called fancy-farming, is often putting his land to more productive use, adding more to the stock of goods and enjoyments than the shrewd tenant farmer alongside who is turning a good penny. He builds more substantial and commodious out-houses, he grows heavier crops, he raises better stock, and he does all this often at no greater *real* cost—that is, with no greater expenditure of labour and consumption of raw material—than the thrifty farmer, but only at greater *apparent* cost or relative—that is, with larger disbursement from his own pocket. But this disbursement represents neither waste of labour nor destruction of material. He pays higher wages to his men, he gives higher prices when he buys, does not drive such hard bargains when he sells, and hands to his overseer as salary that profit which the thrifty tenant keeps as his own overseer. All which means not that there has been no gain from his enterprise, but only that he has allowed his labourers, his customers, and his overseer to divide it among them instead of keeping it for himself. No doubt profit is a most influential factor in determining the course of industry, for capitalists generally will not long continue any course that brings no profit; but for all that, profit is a most delusive test of productiveness. Here is an example in which the influence of profit has diverted and continues to divert one of the most important industries from more to less productive lines.

A farmer employs habitually 10 men at 16s. a week to grow corn, spending thus (in round numbers) £400 a year, as wages, on which outlay he makes a profit of (say) 10 per cent. = £40. For simplicity's sake we leave out of account his other expenses, on which also we may assume him to make

10 per cent. The farmer gets back every year the whole of this £400, besides pocketing his £40. It is clear, then, that the labour of these men must produce from that land every year £440 of wealth, fresh wealth, in the shape of corn; £400 of which goes to them and £40 to their employer. If now the farmer sees his way by laying down his land in grass to get £50 only from it total in the shape of meat, employing his time in looking after his cattle instead of after his men, he will be the gainer by £10 a year. His interest then will be to clear all the labourers (with their families) off the land and lay it down to grass, the land henceforth producing only £50 worth of meat instead of £440 worth of corn. His interest, in short, will be to depopulate the area in his possession, and reduce the productiveness of the land to about one-ninth of what it was. This is the kind of thing that is now actually going on over the most fertile parts of Great Britain, and that has been carried in Ireland to such a pitch as to reduce the population from eight millions to less than five.

INTEREST.—What is interest? Interest, it will be said, is payment for the use of capital. But is all the payment that is made for use of capital, interest? Suppose I have a carriage,[1] and that a borrower hires it for a month and I charge for the use, is the whole of that charge interest?

1. The use to which the borrower will put it will take something out of it. Even if there is no outward appearance of wear and tear when it is returned, still it is certain there must have been wear and tear. The cart is a month nearer to its latter end. I charge something on this account; but it is not interest. I profit nothing by it. It is compensation for deterioration.

2. The borrower may never return my cart at all; he may sell it and bolt, or ruin it and go bankrupt. I charge some-

[1] Adapted from M. Flürschëim.

thing for this also; but it is again not interest but insurance against risk.

3. I may have built that cart, not to use nor to sell, but to let out for hire; and if I charge no more than will, after a series of hirings, recoup me for my labour in collecting the timber and iron and working them up into a cart, the charge I make is again not interest but reward of my labour; *i.e.*, wages.

4. I may have been on the point of using that cart myself when the borrower applied for it, and it will put me to inconvenience or loss to part with it just then. But if he makes it worth my while I may forego my expected profit or enjoyment. I charge then for that; but that again is not interest, but only compensation for a sacrifice. Interest is something over and above compensation. I am none the better off for the lending; I am only squared.

5. But if my cart is standing idle and likely to remain idle for a month, so that it will not hurt me to lend it, provided I am compensated for deterioration and insured against risk, and yet I do charge, over and above this, for the mere permission to use it, because I know that he is in want of a cart, and will pay rather than not have it; *that* is interest. This constant attempt of lenders to take advantage of the necessities of borrowers causes interest and its fluctuations.

If the number of idle carts increase, the number of borrowers and their eagerness to borrow remaining the same, it will be easier for them to get a cart somewhere, and they will therefore be able to get one on easier terms: the rate of interest will fall. Conversely, if the number of borrowers or their eagerness to borrow increase, either because the greater urgency of their work compels them to borrow, or because the increasing profit of carting tempts them to borrow, then the number of idle carts remaining the same, the lenders can exact more; the rate of interest will rise. Interest then arises from the necessities of borrowers, and the tendency of the lender to take advantage of their necessities. The tendency may be quite right and proper; I am not going into the ethics of the question; but whether right or wrong, interest arises thus and in no other way.

If employment were so abundant, and labour so well paid that no one was under any necessity to borrow, interest would disappear. Every one being able to command not only the necessaries of life but its comforts by his own labour, would obtain them in that way rather than pay interest for using them before he had earned them, with the certainty of having to return them unimpaired when he *had* earned them; or if some were so improvident they would be so few, as compared with the amount of capital lying idle, that they would get the use of it for next to nothing.

But what do we mean by this capital on which interest is paid? Do we mean instruments or money? The famous law of indifference will show us.

THE LAW OF INDIFFERENCE.

This law is universally accepted, I believe, by economists. According to this law, as stated by Walker—"In regard to two portions of capital as yet uninvested, there is no reason why one should bear a higher rate of interest than the other"; and accordingly they both bear the same rate. Nothing can be clearer than that the Economist is here adopting the very meaning he repudiates; that by "Capital" he means, as the man in the street means, money and not instruments; and money not as coin but as money-power—as the bank balance or other registered claim that *commands* the coin or goods