

## The Economic Role of Saving and Capital Goods

As the popular philosophy of the common man sees it, human wealth and welfare are the products of the cooperation of two primordial factors: nature and human labor. All the things that enable man to live and to enjoy life are supplied either by nature or by work or by a combination of nature-given opportunities with human labor. As nature dispenses its gifts gratuitously, it follows that all the final fruits of production, the consumers' goods, ought to be allotted exclusively to the workers whose toil has created them. But unfortunately in this sinful world conditions are different. There the "predatory" classes of the "exploiters" want to reap although they have not sown. The landowners, the capitalists, and the entrepreneurs appropriate to themselves what by rights belongs to the workers who have produced it. All the evils of the world are the necessary effect of this originary wrong.

Such are the ideas that dominate the thinking of most of our contemporaries. The socialists and the syndicalists conclude that in order to render human affairs more satisfactory it is necessary to eliminate those whom their jargon calls the "robber barons," i.e., the entrepreneurs, the capitalists, and the landowners, entirely; the conduct of all production affairs ought to be entrusted either to the social apparatus of compulsion and coercion, the state (in the Marxian terminology called Society), or to the men employed in the individual plants or branches of production.

Other people are more considerate in their reformist zeal. They do not intend to expropriate those whom they call the "leisure class" entirely. They want only to take away from them as much as is needed

to bring about “more equality” in the “distribution” of wealth and income.

But both groups, the party of the thoroughgoing socialists and that of the more cautious reformers, agree on the basic doctrine according to which profit and interest are “unearned” income and therefore, morally objectionable. Both groups agree that profit and interest are the cause of the misery of the great majority of all honest workingmen and their families, and, in a decent and satisfactory organization of society, ought to be sharply curbed, if not entirely abolished.

Yet this whole interpretation of human conditions is fallacious. The policies engendered by it are pernicious from whatever point of view we may judge them. Western civilization is doomed if we do not succeed very soon in substituting reasonable methods of dealing with economic problems for the present disastrous methods.

### Three Factors of Production

Mere work — that is, effort not guided by a rational plan and not aided by the employment of tools and intermediary products — brings about very little for the improvement of the worker’s condition. Such work is not a specifically human device. It is what man has in common with all other animals. It is bestirring oneself instinctively and using one’s bare hands to gather whatever is eatable and drinkable that can be found and appropriated.

Physical exertion turns into a factor of human production when it is directed by reason toward a definite end and employs tools and previously produced intermediary products. Mind — reason — is the most important equipment of man. In the human sphere, labor counts only as *one* item in a combination of natural resources, capital goods, and labor; all these three factors are employed, according to a definite plan devised by reason, for the attainment of an end chosen. Labor, in the sense in which this term is used in dealing with human affairs, is only one of several factors of production.

The establishment of this fact demolishes entirely all the theses and claims of the popular doctrine of exploitation. Those saving and thereby accumulating capital goods, and those abstaining from the consumption of previously accumulated capital goods, contribute their share to the outcome of the processes of production. Equally indispensable in the conduct of affairs is the role played by the human mind. Entre-

preneurial judgment directs the toil of the workers and the employment of the capital goods toward the ultimate end of production, the best possible removal of what causes people to feel discontented and unhappy.

What distinguishes contemporary life in the countries of Western civilization from conditions as they prevailed in earlier ages — and still exist for the greater number of those living today — is not the changes in the supply of labor and the skill of the workers and not the familiarity with the exploits of pure science and their utilization by the applied sciences, by technology. It is the amount of capital accumulated. The issue has been intentionally obscured by the verbiage employed by the international and national government agencies dealing with what is called foreign aid for the underdeveloped countries. What these poor countries need in order to adopt the Western methods of mass production for the satisfaction of the wants of the masses is not information about a “know how.” There is no secrecy about technological methods. They are taught at the technological schools and they are accurately described in textbooks, manuals, and periodical magazines. There are many experienced specialists available for the execution of every project that one may find practicable for these backward countries. What prevents a country like India from adopting the American methods of industry is the paucity of its supply of capital goods. As the Indian government’s confiscatory policies are deterring foreign capitalists from investing in India and as its prosocialist bigotry sabotages domestic accumulation of capital, their country depends on the alms that Western nations are giving to it.

### Consumers Direct the Use of Capital

Capital goods come into existence by saving. A part of the goods produced is withheld from immediate consumption and employed for processes the fruits of which will only mature at a later date. All material civilization is based upon this “capitalistic” approach to the problems of production.

“Roundabout methods of production,” as Böhm-Bawerk\* called them, are chosen because they generate a higher output per unit of input. Early man lived from hand to mouth. Civilized man produces

\* Eugen von Böhm-Bawerk (1851–1914), Austrian economist, professor to Ludwig von Mises, renowned for his scholarly study of interest theory, *Capital and Interest*. Böhm-Bawerk also served as Finance Minister in the Austro-Hungarian government, 1895, 1897, and 1900–1904.

tools and intermediary products in the pursuit of long-range designs that finally bring forth results which direct, less time-consuming methods could never have attained, or could have attained only with an incomparably higher expenditure of labor and material factors.

Those saving — that is consuming less than their share of the goods produced — inaugurate progress toward general prosperity. The seed they have sown enriches not only themselves but also all other strata of society. It benefits the consumers.

The capital goods are for the owner a dead fund, a liability rather than an asset, if not used in production for the best possible and cheapest provision of the people with the goods and services they are asking for most urgently. In the market economy the owners of capital goods are forced to employ their property as if it were entrusted to them by the consumers under the stipulation to invest it in those lines in which it best serves those consumers. The capitalists are virtually mandataries of the consumers, bound to comply with their wishes.

In order to attend to the orders received from the consumers, their real bosses, the capitalists must either themselves proceed to investment and the conduct of business or, if they are not prepared for such entrepreneurial activity or distrust their own abilities, hand over their funds to men whom they consider as better fitted for such a function. Whatever alternative they may choose, the supremacy of the consumers remains intact. No matter what the financial structure of the firm or company may be, the entrepreneur who operates with other people's money depends no less on the market, that is, the consumers, than the entrepreneur who fully owns his outfit.

There is no other method to make wage rates rise than by investing more capital per worker. More investment of capital means to give to the laborer more efficient tools. With the aid of better tools and machines, the quantity of the products increases and their quality improves. As the employer consequently will be in a position to obtain from the consumers more for what the employee has produced in one hour of work, he is able — and, by the competition of other employers, forced — to pay a higher price for the man's work.

### Intervention and Unemployment

As the labor union doctrine sees it, the wage increases that they are obtaining by what is euphemistically called “collective bargaining” are not

to burden the buyers of the products but should be absorbed by the employers. The latter should cut down what in the eyes of the communists is called “unearned income,” that is, interest on the capital invested and the profits derived from success in filling wants of the consumers that until then had remained unsatisfied. Thus the unions hope to transfer step-by-step all this allegedly “unearned income” from the pockets of the capitalists and entrepreneurs into those of the employees.

What really happens on the market is, however, very different. At the market price  $m$  of the product  $p$ , all those who were prepared to spend  $m$  for a unit of  $p$  could buy as much as they wanted. The total quantity of  $p$  produced and offered for sale was  $s$ . It was not larger than  $s$  because with such a larger quantity the price, in order to clear the market, would have to drop below  $m$  to  $m-$ . But at this price of  $m-$  the producers with the highest costs would suffer losses and would thereby be forced to stop producing  $p$ . These marginal producers likewise incur losses and are forced to discontinue producing  $p$  if the wage increase enforced by the union (or by a governmental minimum wage decree) causes an increase of production costs not compensated by a rise in the price of  $m$  to  $m+$ . The resulting restriction of production necessitates a reduction of the labor force. The outcome of the union’s “victory” is the unemployment of a number of workers.

The result is the same if the employers are in a position to shift the increase in production costs fully to the consumers, without a drop in the quantity of  $p$  produced and sold. If the consumers are spending more for the purchase of  $p$ , they must cut down their buying of some other commodity  $q$ . Then the demand for  $q$  drops and brings about unemployment of a part of the men who were previously engaged in turning out  $q$ .

The union doctrine qualifies interest received by the owners of the capital invested in the enterprise as “unearned” and concludes that it could be abolished entirely or considerably shortened without any harm to the employees and the consumers. The rise in production costs caused by wage increases could therefore be borne by shortening the company’s net earnings and a corresponding reduction of the dividends paid to the shareholders. The same idea is at the bottom of the unions’ claim that every increase in what they call productivity of labor (that is, the sum of the prices received for the total output divided by the number of man hours spent in its production) should be added to wages. Both methods mean confiscating for the benefit of the employees the whole

or at least a considerable part of the returns on the capital provided by the saving of the capitalists. But what induces the capitalists to abstain from consuming their capital and to increase it by new saving is the fact that their forbearance is counterbalanced by the proceeds of their investments. If one deprives them of these proceeds, the only use they can make of the capital they own is to consume it and thus to inaugurate general progressive impoverishment.

### The Only Sound Policy

What elevates the wage rates paid to the American workers above the rates paid in foreign countries is the fact that the investment of capital per worker is higher in this country than abroad. Saving, the accumulation of capital, has created and preserved up to now the high standard of living of the average American employee.

All the methods by which the federal government and the governments of the states, the political parties, and the unions are trying to improve the conditions of people anxious to earn wages and salaries are not only vain but directly pernicious. There is only one kind of policy that can effectively benefit the employees, namely, a policy that refrains from putting any obstacles in the way of further saving and accumulation of capital.