

lack of information as to prevailing rates of interest and existing degrees of security for the principal.

I remember to have read somewhere an estimate by an economist of reputation, fixing this "disinclination of capital to emigrate" at two per cent. It is doubtful, however, whether the matter is subject to any such form of statement. The disinclination to invest capital abroad must differ among men of different races; it must differ with differing conditions respecting the communication of news, and respecting international relations. Indeed, it must differ widely with differing moods of the public mind. At times, it may disappear altogether under the excitement of speculative mania, as in the days of the South Sea Bubble, and in the year preceding the English crisis of 1825. It sometimes seems to be the case that loans and investments are made abroad more freely than at home, probably because it is less easy to detect the fallacy of schemes bearing foreign names, and relating to distant lands.

CHAPTER IV.

PROFITS.

302. Definition of Profits.—We have now seen two shares cut off the product of industry—rent and interest; two claimants satisfied—the landlord and the capitalist.

We now come to inquire respecting the share of the Employer, who organizes and conducts production, deciding what shall be produced; in what amounts, of what varieties, materials and patterns; and to what persons, at what prices, and on what terms of payment, the products shall be sold.

303. The Entrepreneur or Employing Class.—We have seen that in a primitive state of industrial society the employer does not appear. When, however, the forms of production become many and complex; when the hand-tool is replaced by the machine; when many persons, of various degrees of skill, strength and intelligence, are united in the

same industrial operation; when the materials consumed are gathered from distant lands, and the products, in turn, are distributed widely to consumers not known to the producer, and are sold largely upon credit; when, moreover, a few simple, standard styles give way to ever-varying fashions, in material, in form, in color: in such a state, the employer, the master, the entrepreneur, becomes a necessity of the situation. He performs a function which is indispensable to a large and varied production, and for so doing receives a remuneration which we call profits.

304. Unfortunately, as it seems to me, the entrepreneur or employing function has not been adequately treated, if, indeed, it has been in the smallest degree recognized. English and American economists, in general, have chosen to regard the capitalist as the employer of labor, that is, as employing labor merely because of the possession of capital, and to the extent only to which he possesses capital. We have just now said that, in an early stage of industrial society, the employer does not appear in distinct shape. The possession of capital there constitutes a sufficient qualification for the employment of labor.

In the later stages of industrial development, the mere possession of capital no longer constitutes the sole, or even the main qualification for employing labor. The laborer no longer looks to the employer to furnish merely food and tools and materials, but to furnish, also, technical skill, commercial knowledge and powers of administration; to assume responsibilities and provide against contingencies; to shape and direct production and to organize and control the industrial machinery. So important and difficult are these duties, so rare are the abilities they demand, that he who can discharge these will generally find the capital required. If he be the man to conduct business,* food, tools, and materials will not, under our modern system of credit, long be wanting to him. On the

* "Many employers of labor, in some parts of England more than half, have risen from the ranks of labor. Every artisan who has exceptional natural abilities has a chance of raising himself to a post of command."
—Marshall's "Economics of Industry."

other hand, without these higher qualifications the mere possessor of capital will employ labor at the risk, almost the certainty, of total or partial loss.

The employer, the entrepreneur, thus rises to be the master of the situation. It is no longer true that a man becomes the employer of labor because he is a capitalist. Men command capital because they have the qualifications to employ labor. To men so endowed, capital and labor alike resort, for the opportunity to perform their several functions and to entitle themselves to share in the product of industry. By this is not meant that the employer is not, in any case, or to any extent, a capitalist, but that he is not an employer to the extent only to which he is a capitalist, nor is he an employer at all because he is a capitalist.

305. Use of the word Profits by English and American Economists.—As the English and American economists generally leave the entrepreneur out of their discussion of production, so they leave out of view the share of the entrepreneur in treating of the distribution of wealth. "Profits" come to mean only the remuneration for the use of capital, what we call distinctively interest; or, if it be recognized that the man who organizes and conducts industrial operations receives something over and above the mere return upon that portion of the capital employed by him which he owns in his own right, that something is disparaged by being termed "the wages of supervision and management."

Now it is fundamental in my theory of distribution that the entrepreneur class, the employers of labor, receive a share of the product of industry which is so important, through its amount, that it can not possibly be omitted from consideration, and so widely different in the principles by which it is governed, that the term wages can not be applied thereto without inducing a wholly unnecessary and mischievous confusion of ideas, leading directly to false results.

To the entrepreneur's share of the product of industry I shall strictly apply the term profits. This use of the term, in my judgment, tends to promote clearer conceptions regarding the distribution of wealth in the modern industrial state.

306. Profits a Species of the Same Genus as Rent.—In my opinion, profits thus defined bear a strong resemblance to rent. In this view I follow Archbishop Whately, who, in the appendix to his treatise on Logic, declares that the rent of land is only a species of an extensive genus, although, as he complains, the English economists have treated it as constituting a genus by itself, and have either omitted its cognate species, or have included them under genera to which they do not properly belong. If this view is correct, the principles deduced therefrom will be of very great consequence, not only to political economy, but to social philosophy. Let us, therefore, state again the essential differences between Rent and Interest.

1st. A portion of the land cultivated for the supply of any given market, bears no rent; this we call the no-rent land. The rent paid for any piece of land is exactly measured, in theory, by its excess of advantages in production, over the advantages in production pertaining to the no-rent land. On the other hand, there is not any no-interest capital. It is true that a person lending capital may not only not obtain, in the result, any interest for its use, but may even lose the principal; but this will be due to violence or fraud, to flood or fire or stress of weather, or, else, to the unsuspected incompetency of the borrower to conduct business, all of which we may sum up in the word accident. There is no reason why such accidents should befall one portion of capital and not another, whereas there is a reason, in the nature of the case, why one piece of land should bear a rent and another not; why one piece should bear a high and another a low rent. Theoretically all capital bears interest; and, theoretically also, all capital bears the same rate of interest, exceptions being either, first, apparent only, as when an additional per cent. is charged, not as interest proper, but for the insurance of the principal, or secondly, those arising from the disinclination of capital to emigrate, from the ignorance or inertia of lenders and borrowers, or from the force of laws interfering with contracts of loan.

2nd. It follows that interest forms a part of the price of

all products, but that rent forms no part of the price of agricultural produce (for the demonstration of this theorem, see par. 262), and that the amount received by the landlord, as rent, is not paid either by the agricultural laborer, or by the consumer of the produce.

307. Profits Governed by the same Law as Rent.—Having restated the essential distinction between interest and rent, I shall now undertake to show that profits, the remuneration of the entrepreneur or employer, partake largely of the nature of rent, being a species of the same genus. So far as this is the case, profits do not form a part of the price of the products of industry, and do not cause any diminution of the wages of labor.

The successful conduct of business, under free and active competition, is due to exceptional abilities or to exceptional opportunities. Whether due to exceptional abilities or to exceptional opportunities, my proposition could be equally well established, just as it makes no difference in the theory of rent whether a piece of land owes its superior advantages for the purposes of cultivation to higher natural fertility, or to closer proximity to the market to be supplied. Yet it can not be a matter of indifference to social philosophy, whether the power to command profits be due to exceptional abilities or to exceptional opportunities; and I may, therefore, be pardoned for pausing to point out that the former are far more efficient than the latter, in securing profits.

To justify this assertion it will be enough to refer to the well-known fact that a great majority of all business houses which have achieved notable success have been founded by men who owed almost nothing to opportunity. On the other hand, nothing is more familiar than the spectacle of great houses, deeply founded, which have enjoyed high prestige, wide connections and large accumulated capital, dwindling away little by little, if not brought abruptly to their downfall, under the successors of the original founder, simply because the management which had been strong and brave and wise, became commonplace, purposeless, timid and weak. All this is so familiar that I do not fear that any American, at least,

will question the assertion that exceptional abilities have far more to do with the successful conduct of business, than exceptional opportunities.

Inasmuch as it would make no difference whether profits were due to exceptional abilities or to exceptional opportunities, while the former are, in fact, much the more important factor in the successful conduct of business, I shall, hereafter, for convenience and simplicity, speak of profits as due to exceptional abilities, just as in discussing the question of the use of the land, we speak of rent as due to differences in fertility, assuming, for convenience of illustration, all the fields under view to be in equal proximity to the market.

308. A Theoretical No-Profits Stage of Production.—If the number of men of exceptional abilities were sufficient or more than sufficient to do all the business that required to be done, of all sorts and in all places; if (2) these men, however much surpassing all other members of the industrial society, were among themselves equal in all respects which concern the conduct of business; and if (3) this class, so constituted and so endowed, were distinguished from all not of their class so clearly and conspicuously that no one having these exceptional abilities should fail to be recognized, and no one lacking such abilities in the full measure should esteem himself capable of conducting business, or be so esteemed, for the purpose of obtaining credit, we should have a situation closely analogous to that which we described (par. 255) in the case of a community near which was found an amount of good land, of uniform quality, adequate, or more than adequate, to raise all produce required for the support of the community.

The result would be, either that this class would, by forming a combination and scrupulously adhering to its terms and its spirit, create and maintain a monopoly price for their services in conducting the business requiring to be done, which is so improbable as to be altogether out of our contemplation, or they would, by competing among themselves for the amount of business, bring down its rate to so low a point that the remuneration of each and every one of this class would be practically equal to what he would receive if employed by another.

This, which we might call the "no-profits" stage of industrial society, corresponds closely to the "no-rent" stage in the cultivation of the soil. The persons remaining in the conduct of business would earn their necessary subsistence, but no more. Economically it would make no difference to them whether they did this, as employers or employed.

309.—In fact, however, the qualifications for the conduct of business are not equal throughout all of a sufficiently numerous class. On the contrary, the range of ability is almost world-wide. First, we have those rarely-gifted persons who, in common phrase, seem to turn every thing they touch into gold; whose commercial dealings have the air of magic; who have such insight as almost to seem to have foresight; who are so resolute and firm in temper that apprehension and alarms and repeated shocks of disaster never cause them to relax their hold or change their course; who have such command over men that all with whom they have to do acquire vigor from the contact and work for them as they would not, perhaps could not, work for others.

Next below, though far below, we have that much larger class of men of business, of a high order of talent, though without genius or any thing savoring of magic, whose unqualified success is easily comprehended, even if it can not be imitated: men of natural mastery, sagacious, prompt and resolute.

Then we have the men who, on the whole, do well, or pretty well, in business: men who enjoy a harmonious union of all the qualities of the entrepreneur, though only in moderate degree, or in whom some defect, mental or moral, impairs a higher order of abilities; men who are never masters of their fortunes, are never beyond the imminence of disaster, and yet, by care and pains and diligence, win no small profits from their business, and, if frugality be added to their other virtues, accumulate in time large estates.

Lower down in the industrial order are a multitude of men who are found in the control of business enterprises for no good reason: men of checkered fortunes, sometimes doing well, but more often ill; some of them, perhaps, filling a place that

would not otherwise be filled, but, more commonly in business because they have forced themselves into it under a mistaken idea of their own abilities, perhaps encouraged by the partiality of friends who have been willing to place in their hands the agencies of production, or intrust them with commercial or banking capital. The industrial careers of these men are not peculiarly happy, though the degree in which they suffer from the constant imminence of loss, perhaps of bankruptcy, is very much a matter of temperament. Some take it extremely hard, and when they fall make no effort to rise again; others are irrepressible as Harlequin, jumping up, alert as ever, after being apparently hanged, drawn and quartered by the common executioner.

310. *The No-Profits Class of Employers.*—Now, in my view of the question of profits, we find, in the lower stratum of the industrial order thus rudely and hastily sketched, a "no-profits" class of employers. Notwithstanding all the magnificent premiums of business success, the men of real business power are not so many but that no small part of the posts of industry and trade are filled by men inadequately qualified, and who, consequently, have a very checkered career and realize for themselves, taking their whole lives together, a meager compensation, so meager that, for purposes of scientific reasoning, we may treat it as constituting no profits at all. Live they do, partly by legitimate toll upon the business that passes through their hands, partly at the cost of their creditors, with whom they make frequent compositions, partly at the expense of friends, or by the sacrifice of inherited means. This bare subsistence, obtained through so much of hard work, of anxiety, and often of humiliation, we regard as that minimum which, in economics, we can treat as *nil*. From this low point upwards, we measure profits.

311. *Profits do not form a part of the Price of Manufactured Products.*—If this view of the employing class be correctly taken, it appears that, under perfect competition, that is, where the conditions of a good market are supplied, manufacturing profits, for instance, are not obtained through any deduction from the wages of mechanical labor; and, secondly,

manufacturing profits do not constitute a part of the price of manufactured goods. All profits are drawn from a body of wealth which is created * by the exceptional abilities (or opportunities) of those employers who receive profits, measured from the level of those employers who receive no profits, just as all rents are drawn from a body of wealth, which is created by the exceptional fertility (or facilities for transportation of produce) of the rent-lands, measured from the level of the no-rent lands.

The price of manufactured goods of any particular description is determined by the cost of production of that portion of the supply which is produced at the greatest disadvantage (par. 137). If the demand for such goods is so great as to require a certain amount to be produced under the management and control of persons whose efficiency in organizing and supervising the forces of labor and capital is small, the cost of production of that portion of the stock will be large, and the price will be correspondingly high, yet, high as it is, it will not be high enough to yield to the employers of this grade any more than that scant and difficult subsistence which we have taken as the no-profits line.

The price at which these goods are to be sold, however, will determine the price of the whole supply, since, in any one market, at any one time, there is but one price for different portions of the same commodity. Hence, whatever the cost of production of those portions of the supply which are produced by employers of a higher industrial grade, they will command the same price as those portions which are produced at the greatest disadvantage. The difference, so measured, will go as profits to each individual employer, according to his own success in production.

312. Profits are not Subtracted from Wages.—Do profits, then, come out of wages? Not at all. The employers of the lowest industrial grade—the no-profits employers, as we have

*Prof. Alfred Marshall says: "The earnings of management of a manufacturer represent the value of the addition which his work makes to the total produce of capital and industry."

called them—must pay wages sufficient to hire laborers to work under their direction. These wages constitute an essential part of the cost, to the employer, of the production of the goods. The fact that these wages are so high is the reason why these employers are unable (their skill and power in organizing and energizing labor and capital being no greater than they are), to realize any profits for themselves.

The employers of the higher industrial grades will pay the same wages to their laborers. Why, in equity or in economics, should a laborer who works for a strong, prudent and skillful master, receive higher wages than one whose fortune it is to work for a vacillating, weak or reckless employer. The one laborer is as efficient as the other, and works as hard. The difference in production, which, in the one case allows rent to be paid, and in the other enables the employer to secure a profit, is due to no superiority in the quality of the labor or the capital employed, over that of the labor and the capital employed where no rents or no profits are realized. In the one case it is due to the superior fertility of the land, or its greater facilities for the transportation of produce; in the other, to the superior abilities or opportunities of him who conducts industry.

In the latter case, the employer, paying wages at the same rate to his laborers, and interest, at the same rate, to the capitalist, for so much as he has to borrow, and selling his goods, so far as they are of equal quality, at the same price as the employer who makes no profits, is yet able to accumulate a clear surplus after all obligations are discharged, which surplus is called profits. This is effected by his careful study of the sources of his materials; by his comprehension of the demands of the market; by his steadiness and self-control in the presence of temptations to extravagance or wild ventures; by his organizing force and administrative ability; by his energy, economy and prudence.

313. The No-Profits Employer.—A failure to discern the true relations of profits to wages has led to a mistaken appreciation of the interests of the community, and especially of the laboring classes, regarding the employers of labor.

While the large profits of the successful employer have been the subject of much jealousy, and almost uniformly excite in the minds of the unthinking the sense of personal wrong, there is an entire lack of jealousy exhibited towards the unsuccessful man of business, who often receives a great deal of sympathy from the laboring class.

So far as the sympathy extended towards the unsuccessful man of business is of a personal nature, flowing from a kindly disposition towards the unfortunate, it is, of course, very amiable. But there is reason to believe that this sentiment is not wholly of a good origin, but is quite as largely produced by a misapprehension of economic relations. The laborers appreciate, in some degree, the cares under which the unsuccessful employer labors, the anxieties from which he suffers, the humiliation into which he is occasionally plunged. They know he has a pretty poor time of it on the whole, and they are not envious of him. On the contrary, they use his hard lot to sharpen their envy of the man who reaps large profits from the conduct of business and the employment of labor. They compare the rich rewards of the one, who, perhaps, in time, becomes worth his millions, with the meager recompense of the other, who, at the end of a long life of labor, has little to show for it all; and the comparison tends to heighten the feeling of loss and of wrong with which the gains of the former are contemplated.

If, however, we have rightly indicated the source of profits, not only is the unsuccessful employer deserving of no special economic sympathy, but his conduct of business, his control of labor-force and capital-force is at a great cost to the laboring class, as forming a part of the general community.

We saw that rents were measured upward from the productive level of no-rent land. If, therefore, that level is lowered, rents are, (par. 257) by that fact raised. Similarly, profits are measured upwards from the level of the no-profits class of employers; and any cause which brings incompetent persons into the conduct of business, or keeps them there against the natural tendency of trade to throw them out, increases the profits of the successful employers, as a class, by enhancing

the cost of production and, consequently, the price of that portion of the supply which is produced at the greatest disadvantage. This enhancement of price is at the expense of all who consume the goods so produced; the laboring class equally with others, in theory; probably in fact more than any other, on account of their limited ability to look out for their own interests in retail trade.

314. What Causes Help to Swell the Proportion of Incompetent Employers of Labor?—Shilly-shally laws relating to insolvency do this; bad money does this; truck does this; protection, in my judgment, does this. Each of these causes enables men to escape the consequences of incompetency, and to hang miserably on to business, where they are an obstruction and a nuisance. Slavery, in like manner, enables men to control labor and direct production, who never would become, on an equal scale, the employers of free labor; and it is not more to the inefficiency of the slave than to the incompetency of the master, that the unproductiveness of chattel labor is due.

The lower the industrial quality of free labor, the more ignorant and inert the individual laborer, the lower may be the quality of the men who can just sustain themselves in the position of employers. Men become the employers of cheap labor who would never become the employers of dear labor, and who ought not to be the employers of any sort of labor. The more active becomes the competition among the wages class, the more prompt their resort to market, the more persistent their demand for every possible increase of remuneration, the greater will be the pressure brought to bear upon such employers to drop out of the place into which they have crowded themselves at the cost of the general community, and where they have been able to maintain themselves only because the working classes have failed, through ignorance or inertia, to exact their full terms.

315. Importance of this View of Profits.—It is competent to any person to dissent from the view of the origin and measure of business profits I have presented; but it can not be gainsaid that, if that view be accepted as correct, we have

here the keystone of the arch, which completes the structure and binds together the other members into a symmetrical whole spanning the entire field of distribution. We shall not, however, be able to appreciate all the consequences of this theory, until we have carried our studies through the subject of wages, the remuneration of labor.

316. Getting Rid of the Employer.—In the department of Production we described the function of the entrepreneur, or employer, the person who, hiring labor on the one hand, and borrowing capital on the other, initiates industrial operations according to his own plans, and with a view to his own economic benefit. Coming down to the department of Distribution, we have, but just now, inquired how the contemplated benefit is secured by the employer, and what are the limits of that benefit, which we term profits.

It has been said, in the course of this discussion, that this benefit obtained by the employer, his profits, has been the object of not a little jealousy and envy on the part of the laborers and capitalists to whom he has paid wages or interest. Those wages and that interest the recipients would be glad to see increased by some addition derived from the source from which the employer obtains his profits. This could only be done by the laborers and the capitalists combining to perform the employer's work in production, and thereby becoming entitled, or perhaps we had better say enabled, to claim his share of the product in distribution.

317. Co-operation.—Organized and systematic efforts to get rid of the entrepreneur or employer have not been unknown. Among the many schemes for largely and rapidly improving the condition of the masses of the people, which had their birth in the period of social and political fermentation which we call the Revolution of 1848, none had fairer promise of substantial results than that known by the name of Co-operation.

Generically, co-operation is a term of wide application, and, in its use in political economy, may express the union of industrial agents in production upon any terms and under any system of organization. Since the period referred to, how-

ever, the term has come to have a limited signification, confined to an industrial organization from which the entrepreneur is excluded, and under which the product of industry is again to be divided into three principal shares, instead of four as under the entrepreneur system. I here only indicate the place which co-operation occupies in the scheme of Distribution, postponing the discussion of the scheme to Part VI.

CHAPTER V.

WAGES.

318. Definition of Wages.—We have seen three shares cut off the product of industry. Of the four principal parts* into which that product is divided, under the entrepreneur organization, as existing almost universally in England, and as rapidly extending in the United States, on the continent of Europe, and in all progressive countries, there remains but one to be treated, Wages, the remuneration of labor.

Before seeking the law which governs wages, two distinctions require to be drawn very clearly, distinctions which the reader will need to hold strongly in mind through the whole course of our future discussion, the distinction, *viz.*, between real and nominal wages, and that between the real and the nominal cost of labor.

319. Real and Nominal Wages.—Real wages are the remuneration of the laborer as reckoned in the necessities, comforts and luxuries of life.

Real wages may differ widely, even when nominal wages are of the same amount, by reason of :

- (a) Variations in the purchase power of money.
- (b) Varieties in the form of payment, as when the board of the laborer, the rent of a cottage, the privilege of grazing a

* Certain minor shares in distribution will be treated in the next chapter. For the purposes of the present discussion they may safely be disregarded.