

A 2086

The Cause of Interest



By
A. S. BAYLY

*Read Y.M.
2/31/35*

THE
HENRY GEORGE LEAGUE OF SOUTH AUSTRALIA
George Parade, off 11 Carrington Street, Adelaide

ONE PENNY

4129

THE CAUSE OF INTEREST

By A. S. BAYLY.

A friend has asked me to define "how much of the product of an orchardist is Rent, how much is Wages, and how much is Interest?" The question has provided an admirable opportunity for presenting a theory as to the cause of interest, and at the same time linking it up with the other two shares of production, namely, wages and rent, in such a manner as to give to readers an introduction to some elements of political economy.

The ancients denied that interest rested on any justifiable foundation, and their view is also shared by a considerable number of modern people. Aristotle declared it unjust; Cicero went so far as to class it with murder; whilst throughout the Middle Ages it was condemned by the Church and prohibited by statute. In fact, what is now called interest was then described as usury, a term which in modern times has been limited to mean the taking of inordinate or excessive interest. Numerous economists still regard the subject of interest as an unsettled problem, and consequently it is not surprising that many people may be found condemning the taking of interest as an exploitation of laborers by capitalists.

Unfortunately politico-economic terms are used in every day speech in quite a different sense from the sometimes limited and sometimes extended meanings attached to them by economists, whilst there is also

some divergence in the meaning of the terms among the economists themselves. It has therefore seemed necessary, in order to avoid misunderstanding, to begin by clearly defining the meaning intended by the author in the terms used in this article.

The fact is patent to all that, "by his constitution, man is beset by physical wants, on the satisfaction of which depend not only the maintenance of his physical life, but also the development of his intellectual and spiritual life." The satisfaction of these wants is dependent on man's own exertions in applying his energy on the material suitable to his needs. This material is land. Man is a land animal, who can only live on and from land, and can use other elements such as air, sunshine and water, only by the use of land.

To state the matter briefly, it may be said that:— From LAND does LABOR using CAPITAL (a part of wealth) produce all WEALTH, which is distributed or shared among the factors or agents of production as RENT (the landowners' share), WAGES (the laborers' share), and INTEREST (the capitalists' share).

By LAND is meant all nature accessible to man (except man himself and his production), including all mineral, vegetable and animal matter, all chemical affinities and natural forces as they exist apart from the modifying influences of man.

By LABOR is meant all human energy directed to the production of wealth in the politico-economic sense. (Some human energy is directed, not to the production of wealth, but to the grabbing of wealth produced by others. Such energy is not labor in the politico-economic sense, though the effect from the viewpoint of individual economy might be the same.)

By CAPITAL is meant that part of wealth which is USED to aid in the production of more wealth, or, as some economists express it, wealth consumed productively.

Hence all capital is wealth, though not all wealth is capital. In order that wealth may partake of the nature of capital it MUST BE USED to aid in the production of more wealth. Thus machinery, buildings, seed-wheat, cattle and all wealth, which instead of being directly consumed in the satisfaction of desire, is devoted to the production of more wealth, is capital. When, for instance, instead of consuming eggs, a poultryman devotes such eggs to exchange (per medium of money or without money) in order to obtain greater satisfaction in the form of a variety of foods, clothing, etc., such eggs are capital. In fact, ALL WEALTH IN EXCHANGE IS CAPITAL. This fact should never be forgotten, for not only will it be found to explain why interest exists and is willingly paid by borrowers to lenders, but if we remember also that a capitalist is simply an owner of capital (be it ever so little), and that every person in a civilized community who devotes wealth to exchange by buying commodities is thus a capitalist, we shall have done much to dispel the "bogey" capitalist which socialists use to frighten economic children.

By WEALTH is meant tangible objects (or parts of land) which have been so secured, moved, combined or altered in form or place and stored up by human energy (labor) as to fit them for the satisfaction of human wants.

If men lived in the same way as the lower animals, by simply taking the spontaneous offerings of nature for the satisfaction of immediate desire without storing up to provide satisfactions for recurring desire, there would be no need for a science of wealth. But man, out of respect for future desires, does store material objects adapted to the satisfaction of such desires, and such stored objects are wealth. Hence, the essential character of wealth is that of human energy, service or labor stored up, as it were, in

material objects so that it might yield satisfaction to desire. It is important to note here, in relation to the subject of interest, that in some forms of wealth, such as grain and cattle, there is stored also, vital and reproductive energy, which no amount of human labor or ingenuity has been able to call into existence.

By PRODUCTION is meant all the processes by which natural objects are changed in form or place (by labor using capital), so as to store up human energy and natural forces in the shape of wealth.

* * * * *

Now wealth, when produced, belongs to, is proper to, or is the property of the factors or agents engaged in its production (namely, landowners, capitalists and laborers), in proportion to the part played by such factors or agents in the process of production.

RENT is the name given to the share of the wealth produced which is proper to or the rightful property of landowners by virtue of the part played in production by land.

WAGES is the name given to the share which is proper to laborers by virtue of the energy exerted by them in production.

INTEREST is the name given to the share which is proper to capitalists by virtue of the increase which can be attributed to their capital as distinct from the shares proper to or due to land and labor.

Unless it can be shown that capital does yield an increase over and above what can be attributed to either land or labor, then there can be no JUSTIFIABLE foundation for interest, no right of property attaching to capitalists by virtue of their ownership of capital. But if it be shown that capital does yield such an increase, then interest is justly or rightly the property of capitalists. Let us, therefore, make an

examination of the processes of production in order to determine the part played by capital.

* * * * *

In analysing the processes of production Henry George found that they could be classed under three categories or modes, which he named respectively as:

- (1) ADAPTING.
- (2) GROWING.
- (3) EXCHANGING.

By "adapting" is meant those processes of production in which we change the form or place of what might be considered the inert matter of nature, as in hunting and fishing and all branches of manufacture. It should be noted, however, that much of the higher branches of manufacturing have become possible only through the third mode, called "exchanging," as will later be shown.

By "growing" is meant those processes of production in which we direct the vital and reproductive forces of some forms of capital (such as grain, seed and cattle) as in agricultural and pastoral pursuits. In this reproductive mode the wealth, which partakes of the nature of capital, is distinguished in character by the vital energy peculiar to living things—an energy which, when adapted to its environment by labor, continues the process of production whilst labor sleeps or is otherwise engaged. This, then, is a clear case in which capital yields an increase over and above what can be attributed to labor—an increase, of which the owner has been able to receive some part at least under the name of interest or usury—in spite of the statutes designed to prohibit such payments—simply because, whoever has the use of such capital in production may receive the increase, and consequently the competition to obtain the use of such capital necessarily leads to the payment of some part

of the increase to the owner by the borrower. But even should there be no borrowing, the increase yielded by this mode is received by the owner as owner and not as user, and is still interest, or the part of wealth attributable to the reproductive forces of capital in production.

By "exchanging" is meant the processes of trading, buying and selling, which became necessary to permit of the more intensive use of the factors land and labor in production, by concentrating upon the most suitable production for which any given piece of land is naturally adapted, and by allowing the division of labor and concentration of effort in specialised industry so as to tremendously increase the skill of laborers over what could be attained by attempting to be "Jacks-of-all-trades" and thereby failing to master any. This mode binds men together in society (through exchange) in a great co-operative effort in which individual mental faculties are given scope to increase individual skill and develop or invent all manner of improved processes in production. Thus, "exchanging" consists in utilising the co-operative reasoning faculties of man or what might be termed "the productive force of civilized society"—a force which is not characteristic of segregated or individual labor, and cannot, therefore, be claimed by individuals as a force or factor in production entitling them to the increased production under the name of wages.

A little consideration will show that this mode of production is by far the most important of all modes—without which, indeed, production could not have reached a stage much in advance of that of primitive barbarism. It requires little imagination to see that without exchange, the "division of labor," with the concentration and co-operation it involves, would be impossible: that without exchange, the accumulation of knowledge transferable by writing or similar means,

must have been small indeed; that without exchange, we would never have been able to call to our aid natural forces such as steam and electricity, nor have invented the wonderful machinery, the shipping, the railways and the numerous improved processes which characterise the production of modern civilized society. So clear is it that exchange or trade is the great civilizer binding man closer and closer in society and raising him from the martyrdom of barbarism and ignorance, that he, who gives the matter the slightest thought, must be lost in wonder at the tariff barriers, the so-called "Protection" and numerous restrictions and licences that are allowed to stand in the way of freedom in exchange among civilized men, who flatter themselves upon their superior knowledge, which could not possibly have been obtained without the exchange they seek so foolishly to restrict.

Now the great benefits of this mode of production spring from what I have called "the productive force of civilized society," a force which, in effect, is analogous to the vital and reproductive forces inherent in the capital utilized in the mode called "growing." And since the benefits of the productive force of society are obtainable only through exchange or trade, the increased production resulting from this mode primarily attaches to the wealth exchanged, that is to say, to capital.

If it be remembered that the essential character of wealth, and therefore of capital, is that of labor and natural forces stored up in material form, then it may clearly be seen that what, for the sake of convenience, has been called interest, is in reality a form of wages, namely, the wages of the labor thus stored up in material form, that is to say it is the wages of the owner of the capital as distinct from the wages of the user of such capital.

In the final analysis, there are but two primary

and essential factors in production, namely land and labor, for the third factor, capital, is a secondary factor, being a composite of the two primary factors land and labor. For, as previously pointed out, the essential character of capital is that of labor or human energy stored up together with natural forces and matter drawn from land. But since capital is not merely human energy (labor) nor merely natural forces and matter (land) it is more convenient to speak of the third factor as "capital" rather than as "a composite of land and labor." So also is it more convenient to speak of the production resulting from capital as "interest" rather than "the wages of the owner of capital." It matters little what name we use to describe anything, so long as the name is convenient and generally understood.

But it is not enough merely to define economic interest as "the wages of the owner of capital," for it may be objected that capital does not of itself begin production, but must be used by labor, and therefore, it is necessary to show that the increased production accompanying the use of capital is not wholly due to the USER but that some part of the increase is yielded by the forces stored or inherent in the capital itself.

Now in the mode of production called "adapting" when we use tools or implements (capital) to change the form or place of inert matter, production proceeds only so long as the user of such tools is actively engaged, and as soon as the user or laborer downs tools with the blow of the whistle, production stops. Such production is evidently, therefore, solely dependent on labor and primarily will all go to labor as wages.

But in the second mode, in growing wheat, or keeping an orchard, or breeding cattle, all that labor can accomplish is to "adapt" the soil or environment necessary for the functioning of the vital and repro-

ductive forces of the seed or trees or cattle, and having done so much the laborer or user of such capital can do no more but simply wait for the natural forces in the capital to yield their increase, which they do at the end of a period of time, during which the laborer may engage in other modes of production, or he may sleep, but he cannot hasten the processes of growing or breeding so as to obtain two or more crops in the time necessary for one. In such case, clearly the increase is in part due to the inherent forces of the capital and in part due to the energy of the user or laborer.

Again, in the third mode called "exchanging" all that the laborer or user of capital can do is to "adapt" by changing the place of material objects or transporting. For the rest he is dependent upon what I have called "the productive force of civilized society," the benefits of which are obtainable only through exchange. Two parties are always necessary in exchange, the buyer and the seller, and if through some means, such as causes the phenomenon called an industrial depression, buyers become relatively scarce and "the productive force of civilized society" is thereby weakened, then the seller may engage in transport to the same extent as before the depression, but the results attending his part of the job will be very different indeed. Strikes, lock-outs, revolutions, wars, unjust distribution of wealth, tariff-barriers, misnamed "protection," and all social maladjustments are negations of society which cause industrial depression by weakening the productive force of society, a social force which can no more be attributed to the individual laborer than can the vital energy which exists in a grain of wheat.

Transport and banking are the chief media of exchange, but to increase the number of miles over which goods are transported, or to increase the number of money tokens or ledger entries, would not

make us any richer in material satisfactions. The benefits of exchange are not in the means of exchange, but in the increased productive force of society obtained through the more intensive use of land and greater concentration of skill, which exchange alone makes possible. And so the causes of industrial depression are not to be found in our methods of transport and banking so much as in the social maladjustments which make for insecurity of the individual members of society through an unjust or inequitable distribution of wealth that reflects itself in the inability of some classes to engage in exchange.

Thus Interest springs from the part played in production by the vital forces in living capital and the productive force of civilized or co-operative humanity available through exchange. The increase given by these forces is shared partly by the user (labor) and partly by the owner (the capitalist) and largely by the landowner.

Now, as has already been pointed out, the increased production resulting from exchange is tremendous. But because transport plays so large a part in the processes of exchange, and in order to secure economy in the effort or labor necessary in transport, the business of exchange tends to concentration, to the building of great cities with enormous populations, and consequently tends to make the land on which the business of exchange is conducted highly productive. And since, as all economists agree, the excess of productivity of any land above the margin of production will be appropriated by landowners as rent, a very large portion of the benefits arising from "the productive force of society" will go to enhance the values of city lands or to increase Rent.

Laborers and Capitalists can only share as Wages and Interest what can be obtained from the best land available to them without the payment of rent, that is to say, from land at the margin of production.

Of what can be produced by labor and capital at the margin of production, capitalists will obtain as their share not more than the average rate of increase attaching to capital used in the reproductive modes of growing and exchanging, and certainly not less than is necessary to replace their capital. The point between such limits at which the "current" rate will settle is determined by the "higgling" of the market or the law of demand and supply.

It is only necessary to add, that as the margin of production falls lower, wages and interest will fall, and rent will rise; whilst if from any cause the margin of production should rise, then both wages and interest will rise and rent will fall.

Thus the reply to my friend's question is, that the proportions of the product from the orchard in question which will constitute Rent, Wages and Interest respectively depend on the margin of production. If the orchard be situate at the margin the whole product will be divided as wages and interest, the interest being determined as indicated, and all over that amount will be the wages of the labor expended. If the orchard is at a point above the margin of production, the excess of productivity at that point above the productivity at the margin will be rent and the balance will be shared as before between wages and interest.

The belief that the payment of interest involves a robbery of labor is probably due to the failure to discriminate between what is properly called interest on capital and the gains accruing to individuals from other sources than the use of capital. Nothing can be properly called capital except articles of wealth actually used to aid in further production of wealth; and nothing can be properly called interest except the increase (over and above what can be attributed to land and labor) which capital yields through the functioning of its reproductive forces.

It is common in the speech and literature of to-day to call everyone a capitalist who possesses anything (independent of his labor) that will yield him a return; whilst such returns are also improperly thought of as interest.

When chattel slavery was a recognised legal institution, the results of slave labor were generally considered as interest on the money expended in the purchase of slaves. It may clearly be seen that the gains of a slave-owner cannot be attributed to the functioning of capital in production, but that they arise from the legalised privilege of the slave-owner to rob the slave of the product of his labor (wages), and cannot, therefore, be properly spoken of as interest.

Under the existing system of land tenure which recognises private ownership of land and private appropriation of its rent, enormous sums are advanced under mortgage to purchasers of land. But though the returns to mortgagees in such transactions are generally spoken of as interest, careful analysis will show that advances for the purchase of land are not really advances of capital; that production is not increased nor the productivity of land in any way affected by its sale and purchase; and that the gain of the mortgagee is not interest, but a share in the rent of land. Wealth devoted to the purchase of land is not used to aid in the production of wealth; that is to say it is not capital, and consequently the returns for advances for the purchase of land cannot be interest.

It cannot be too often repeated that nothing can be capital that is not wealth—that does not consist of tangible objects produced by labor from land, which have in themselves, and not by proxy, the power of ministering to desire or of being used as an instrument in production.

A government bond, for instance, is not capital nor in some cases even the representative of capital. The

wealth that was once received by the government that gave the bond may have been consumed unproductively by being expended in warships, cannon, munitions, and in keeping men marching, killing and destroying. In such cases the bond does not represent capital at all, but is simply a solemn declaration that the government will take so much wealth from the existing stock of the people and turn it over to the bondholder.

Hence it may be seen that the very large sums paid by governments to bondholders and described as interest on the public debt is not interest at all—is not an increase yielded by capital in production, but the gain of one section of the people at the expense of another section.

Public debts are merely devices adopted by governments to obtain control over existing wealth by promising the owners who give it up that other people shall be taxed to pay them, and that other people's children shall be taxed in the future for the benefit of their children. Unscrupulous and spendthrift governments find in the institution of public debts an easy means of obtaining wealth which they could not so readily obtain by immediate taxation without arousing a storm of protest and resistance.

Among the evil effects of public debts may be counted government extravagance and corruption, whilst the burden of taxation upon industry for the purpose of paying so called "interest" to the bondholders has become intolerable; has resulted in widespread unemployment by reducing the purchasing power of the masses; while there is everywhere to be heard suggestions for repudiation, for reduction of "interest," or inflation of the currency, to lighten the burden of these iniquitous devices, which threaten to collapse by virtue of their own weight.

So long as our recognised economists, who grace the chairs of "economics" in our universities, fail to point

out and emphasise the distinction between interest and what is properly called legalised robbery, so long will the masses of the people continue to denounce interest, or at least demand some legislative control or reduction of interest.

True economic interest cannot be abolished except by the destruction or the discontinued use of capital. Nor can the rate of interest, which depends on the rate of increase or growth of capital at the margin of production, be "fixed" by legislative enactment.

Those who, seeing the want and misery, the vice and crime resulting from an unjust distribution of wealth (that is so abundant as to be deemed by many as over-produced) may see, if they look carefully, that the remedy lies, not in the abolition or attempted control of interest, but in the cancellation of legislative enactments which give to certain sections of the community a special privilege or power to appropriate the wealth of others.

I have defined rent as the share of production proper to, or the rightful property of, landowners by virtue of the part played in production by land. Whoever gives the matter consideration will readily see that the land of any country is a gift of nature to the people of that country and its rent is, therefore, proper to or the rightful property, not of a privileged section, but of the whole community.

Appropriate by taxation the ground rent which rightfully belongs to the community that creates it; abolish the taxation which takes wages and interest from those who produce them by their industry, rid society of the burdens of landlordism and public debts, and interest can be safely left to capitalists as a beneficent addition to the wealth produced by their labor. For then all men would be capitalists and all would share interest.