

# NATURAL LAW, MARGINAL PRODUCTIVITY, AND THE JUST WAGE

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## ABSTRACT

The Church's insistence on a just wage seems to contradict economic science, which allocates all incomes according to an invariant rule of marginal utility, a rule that is supposedly derived from the natural law. Clearly, either the Church or the economists have misinterpreted the natural law. Pre-capitalist theories rooted the distribution of incomes in concepts of distributive justice based in Aristotle and refined by the Scholastics. Neoclassicism did away with distributive justice by rooting all theory in corrective justice alone. This paper examines the history of the question, from Aristotle to Keynes, and offers a critique of marginal theory's failure either to provide distributive justice or to describe accurately any actual economy. It then attempts to root the just wage in the natural law by re-establishing distributive justice as the core of all rational economic theory.

## FROM JUSTICE TO "NATURAL LAW"

### *IRRECONCILABLE DIFFERENCES*

When we look at the tensions between Catholic teaching and capitalist practice, we cannot escape the conclusion that the two seem to have irreconcilable differences. On the one hand, we have the claims of a "positive" science, deemed as certain as astronomy or physics, which claims to distribute incomes according to a "natural" and inflexible law that excludes all human intentionality. On the other hand, we have an ecclesial authority which places a purely moral requirement on the distribution of incomes, namely the Just Wage. At this point the question becomes categorical: Either incomes are distributed by "automatically" operating "natural law" or they involve human intentionality based on a concept of justice; there would seem to be no

middle ground. It is impossible that a natural phenomenon could be modified by a moral diktat; the decree of the pope cannot place the sun at the center of the universe.

Yet, on another level, this conflict is surprising; it is absolutely incomprehensible that justice could be in conflict with the natural law, or indeed that justice itself could be anything but a foundation for the natural law, at least insofar as that law deals with human actions. Further, a "natural law" which displaces the moral law would itself be unnatural and self-contradictory, unless we are willing to conclude that morality is unnatural. Therefore, we can conclude that either the natural law in this case has been misunderstood or that the Just Wage isn't a part of the moral law at all. This statement of the problem excludes as merely heretical the rather neat solution of the problem contained in the doctrine of the double truth. The most

recent advocate of this doctrine is Alejandro Chafuen, who posits that there are *two* distinct sets of natural laws, the “analytic” and the “normative.”<sup>1</sup> The analytic natural law is the law of nature and the normative law, the rules of conduct.<sup>2</sup> The analytic natural law describes a strict unvarying regularity that holds in nature. Economic law, for Chafuen, falls under the “analytic” natural law, and hence “*no ethical judgment can invalidate an economic law.*”<sup>3</sup> Therefore, economics is sovereign and “value-free.”<sup>4</sup> But this view of nature merely posits a world at war with itself. While such an irrational dualism is certainly a theoretical possibility, it is not a possibility at all for those committed to working within the Christian tradition. If, therefore, we exclude a world in which the natural law is at war with itself, then we must assume that there is an error in this case that resides either in the statement of the economic law or in the statement of the moral law.

Our task then is to locate the error, and our method must be to examine the roots of both theories. For the Church’s view, these roots are in the Aristotelian-Scholastic concept of justice, and for marginal productivity, these roots are in utilitarian economics.

#### ARISTOTLE

For Aristotle, justice is not just a part of virtue, but “virtue entire, nor is the contrary injustice a part of vice, but vice entire” (*Nicomachean Ethics*, 1139a,

10).<sup>5</sup> Justice underlies all the virtues and deals with the relations of man and man:

And therefore justice is often thought to be the greatest of virtues, and “neither evening nor morning star” is so wonderful; and proverbially “in justice is every virtue comprehended.” And it is complete virtue in its fullest sense, because it is the actual exercise of complete virtue. It is complete because he who posses it can exercise his virtue not only in himself, but towards his neighbor also (*Ethics*, 1129b, 25).

In other words, justice puts us in right relationship not only with ourselves, but also with our fellow man. Hence, it governs all social relations. In is within this relationship of man to man, that is, within justice, that Aristotle locates economics. He presents a sophisticated analysis that includes a demand function, a distinction between use and exchange values, the function of money as the medium between value and demand (or “need”), and usury, among other things. Aristotle begins his reflections with the family, for “The family is the association established by nature for the supply of men’s everyday wants” (*Politics*, 1252b, 11).<sup>6</sup> It is the family, and not the individual that is the starting point of economic thought because only the family is self-sufficient; an individual in isolation can neither reproduce nor provide for himself (*Politics*, 1253a, 26). Man, for Aristotle, is a social being always using language and reason and always embedded in a

<sup>1</sup> Alejandro A. Chafuen, *Faith and Liberty: The Economic Thought of the Late Scholastics* (New York: Lexington Books, 2003) 20.

<sup>2</sup> Chafuen, *Faith and Liberty* 20.

<sup>3</sup> Chafuen, *Faith and Liberty* 24.

<sup>4</sup> Chafuen, *Faith and Liberty* 25.

<sup>5</sup> Aristotle, “Nicomachean Ethics,” trans. W. D. Ross, *Introduction to Aristotle*, ed. Richard McKeon (New York: Modern Library, 1947), vol.

<sup>6</sup> Aristotle, “Politics,” trans. Benjamin Jowett, *An Introduction to Aristotle*, ed. Richard McKeon (New York: The Modern Library, 1947), vol.

cultural milieu. Part of man's social nature is the social nature of production; nearly all production is a social process. As a social relation, production is governed by the rules of justice, rules which Aristotle divided into *distributive* and *corrective* justice.

*Distributive* justice deals with how society distributes its "common goods." Aristotle defines this as "things that fall to be divided among those who have a share in the constitution" (*Ethics*, 1130b, 31-33). This refers to the *common* goods of a state, a partnership, corporation, or some cooperative enterprise. For Aristotle, these things should be divided by "merit" based on contributions, but what constitutes this merit will be a matter that is determined culturally, "for democrats identify it with the status of freeman, supporters of oligarchy with wealth (or with noble birth), and supporters of aristocracy with excellence" (*Ethics*, 1131a, 25-29).

*Corrective* justice,<sup>7</sup> on the other hand, deals with "justice in exchange"; that is with transactions between individual men. In this case, justice consists in exchanging equal values, in "having an equal amount before and after the transaction" (*Ethics*, 1132b, 19-21). The problem is how to determine equal values among dissimilar products, which is nearly always the case. To use Aristotle's example, how many pairs of shoes are equal to one house? The only way to know this is by "need," which

many economists understand as the demand function mediated by money. Thus, the demand for houses and shoes can be compared by looking at their prices and the two can be equated in terms of money. Money, however, is a social convention: "this is why it has the name money (*nomisma*)— because it exists not by nature but by law (*nomos*)" (*Ethics*, 1133a, 25-31). Thus, the requirement for equality in exchange comes from the natural law, but the method of implementing it is legal or conventional.

Distributive justice, then, is a distribution of the products of a group to the members of the group; corrective justice is an equal exchange between individuals. Distributive justice will be proportional to one's contribution to the group, and hence there can be unequal distributions based on unequal contributions; the measurement of contribution will always involve a judgment and be dependent on the cultural context; it cannot be reduced to a formalistic calculation. Corrective justice, on the other hand, will always involve equal amounts, like for like. Distributive justice is logically prior to corrective justice, since goods must be distributed from production before they can be exchanged. The distinction between distributive and corrective justice remains central to economics, even if economists do not always recognize the connection. Indeed, the question of distributive justice has disappeared completely from neoclassicism; neoclassical economists generally cast economic questions in terms of free exchanges, that is, in terms of corrective justice. This limits the kind of questions they can ask. In the case of wages, for example, we need to know if factor shares—the amounts of compensation given to land, capital, and

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<sup>7</sup> During the Middle Ages, the term "corrective" justice became "commutative" justice due to a mistranslation. The word Aristotle uses is *διόρθωτικός* (*dióρθotikós*), "corrective" (LSJ). Although the term "commutative" has become more common, we will use the term "corrective" as closer to the original sense in Aristotle.

labor— are a question of distributive justice or of corrective justice. If the former, the shares will be determined by merit, which itself is culturally influenced; if the latter, shares will fall under a calculation of the demand curves for labor and capital. Answering the question solely in terms of corrective justice suits the individualistic premises of neoclassicism because corrective justice is only concerned with exchanges between individuals; “social” questions do not intrude themselves. Therefore, the notion of a social (distributive) justice does not arise. Distributive justice, on the other hand, is always a matter of merit and contribution, questions that are answered in a social context.

#### *ST. THOMAS AQUINAS AND THE SCHOLASTICS*

St. Thomas synthesized the work of Aristotle with a specifically Christian point of view to produce an economic view that reigned until the 17<sup>th</sup> century. Underlying his economic theories were two fundamental assumptions: “that economic interests were subordinate to the real business of life, which is salvation, and that economic conduct is one aspect of personal conduct, upon which, as on other parts of it, the rules of morality were binding.”<sup>8</sup> Economic activity was regarded as a strong passion that needed restraint and boundaries; it needed to be put in its place, a place described by St. Thomas:

It is lawful to desire temporal blessings, not putting them in first place, as though setting up our rest in them, but regarding them as aids to blessedness, inasmuch as they support our corporal

life and serve as instruments for acts of virtue (*ST II-II*, 83, 6).<sup>9</sup>

Here we have a view of economics as *bounded*, as existing within some limits. For example, self-interest, the mainspring of modern economics, was neither unknown nor condemned by the Scholastics. Indeed, it was required, since every man was required to provide for himself and his family.<sup>10</sup> However, self-interest was *limited* to providing the goods necessary for oneself and one’s family only to the level called for by their “station in life”; beyond that, self-interest becomes the vice of greed.<sup>11</sup> The bounds of economics were given by Aristotle’s idea of natural and unnatural exchange, the natural being that which supplies our needs, but the unnatural is that for profit itself alone, unrelated to actual needs (*ST II-II*, 77, 4).

Thus, Thomas combines two ideas, the idea of a proper “station in life” with the idea of justice in exchange to provide a synthesis between distributive and corrective justice. It is just this combination which, as we shall see, is often missing from neoclassical economics.<sup>12</sup> The idea of proper

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<sup>9</sup> St. Thomas Aquinas, “Summa Theologica,” trans. Fathers of the English Dominican Province, (Allen, Texas: Christian Classics, 1981), vol., 5 vols.

<sup>10</sup> Mary L. Hirschfeld, Standard of Living and Economic Virtue: Building a Bridge between St. Thomas Aquinas and the 21st Century, 2005, Available: [http://www.nd.edu/~econplcy/workshops/documents/jsce\\_paper.pdf](http://www.nd.edu/~econplcy/workshops/documents/jsce_paper.pdf), December 17 2005.

<sup>11</sup> Hirschfeld, Standard of Living and Economic Virtue.

<sup>12</sup> Albino Barrera O. P., Modern Catholic Social Documents and Political Economy (Washington, D.C.: Georgetown University Press, 2001) 57.

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<sup>8</sup> R. H. Tawney, Religion and the Rise of Capitalism (New York and Toronto: Mentor Books, 1954) 34.

“stations” in life shows that equality was not a goal of Scholastic economics; while a race of sinless men could live from a common purse, communism was left behind in the garden.<sup>13</sup> The “stations in life” were embedded in a cultural milieu which required a hierarchy. The mechanism by which the Scholastics attempted to unite the distributive and allocative functions was the Just Price.

The Scholastics were aware of all the elements that go into modern pricing theory: utility, scarcity, supply and demand, costs, etc. However, they refused to reduce price to mere economic calculation. Most specifically, they refused the mainspring of modern pricing, utility, or “usefulness to the buyer.” As one of the later Scholastics, Louis Molina, put it,

That one may not accept a higher price by reason of the advantage of gain of the buyer is proved from the fact that the advantage is not something of the seller's but the buyer's; therefore the seller may not accept payment for it; otherwise he would sell what is not his (1759, *Disputation*, 348:6).<sup>14</sup>

Molina is repeating the words of Thomas from five centuries earlier, and the rejection of utility pricing is fairly consistent across the centuries dominated by Scholasticism. But if not utility, then what is the basis of the just price? For St. Thomas it is a matter of a price that “is neither more nor less than the worth of the thing” (*ST*, II-II, 77, 1). But the worth of a thing is “not fixed

with mathematical precision,” but “depends on a kind of estimate, so that a slight addition or subtraction would not seem to destroy the equality of justice” (*ST*, II-II, 77, 1, r. 1). Thomas does not explicate the basis of a just price because the practice is already a part of the economic system of his time and he assumes his audience already knows what he is talking about.<sup>15</sup> What seems hopelessly imprecise to us was more or less accepted as a “natural” part of the pricing system. Indeed, no pricing theory, right to our own day, has ever succeeded in being precise. The Scholastics insisted that price reflect the wider social concerns expressed by the phrase, *common estimation*. Common estimation is not a result of market concerns, although it considered those concerns. Rather, it is an ethical judgment about price that preceded the market; it is “an ethical judgment of at least the most influential members of the community.”<sup>16</sup> In general, the Scholastic writers preferred prices that were fixed by law with due account given to market conditions; they were unwilling to give free reign to the market alone. The

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<sup>15</sup> George O'Brien, *An Essay on Medieval Economic Teaching* (Kitchner, Ontario: Batouche Books, 2001) 59.

<sup>16</sup> O'Brien, *An Essay on Medieval Economic Teaching* 64. There have been attempts to equate the “common estimation” with the market price so that the just price is “just the price” fixed by the free market. See, for example, the Chafuen work previously cited. However, this thesis is hard to credit, not only in the light of the specific denial of utility pricing, but also for the fact that if common estimation and market price were the same, then the vast literature of the Scholastics on the subject would be merely tautological.

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<sup>13</sup> Jarrett Bede, *Social Theories of the Middle Ages: 1200-1500* (Westminster, Maryland: The Newman Book Club, 1942) 122.

<sup>14</sup> Bernard W. Dempsey S. J., “Ability to Pay,” *Review of Social Economy* LXIII.3 (2005): 341.

market was not sovereign, but constrained.

The primary factor in the common estimation is the wages of the workmen involved with the product, including the “worker” who is the merchant selling it. Just price theory is very much opposed to what is now called “economic profit”; the merchant is entitled to earn enough to support his station in life, but no more. His work deserves compensation, as does anyone’s. At the same time, the worker is entitled to support adequate to his “station in life.” Therefore, wages are related to the needs of the worker or the vendor, rather than a utilitarian valuation of the output.<sup>17</sup> The idea of the just price, from an economic standpoint, is that there should be no wealth without work, and that prices should be driven to costs, including and especially the cost of labor. Therefore the just price theory is often considered a precursor of the “labor theory of value” favored by Adam Smith and David Ricardo.

The theory of the just price conformed to the general practice of the middle ages which was to have a “free market” in natural produce (wheat or wool, for example) while attempting to control the rate of profit and wages. This control was exercised through the guild system and through positive law by setting fixed prices. The guilds themselves were associations of masters and journeymen that were granted monopolies over some trade in a given area in return for the pledge of a consistent level of quality and a fair

price. Being monopolies, they were carefully watched.

Thus, the just price was an attempt to drive price to the costs of production and eliminate what we would now call “economic rents.” Modern theory finds the notion of a just price somewhat quaint and, to the extent that prices were fixed by law or monopolies, somewhat threatening. However, it should be noted that both modern and medieval pricing make the same claims, namely the elimination of unjust profits or economic rents by driving prices to costs; it may be equated with what is called the “long-term equilibrium price.”<sup>18</sup> But the medieval theory makes another claim missing from modern pricing, namely that both the merchant and the laborer will receive adequate compensation to support them in their stations in life, stations assigned by cultural forces. There would not be equality, but neither would there be massive wealth on one hand or destitution on the other; some notion of the common good would rule all classes.

#### *THE ENLIGHTENMENT*

Between the 15<sup>th</sup> and the 18<sup>th</sup> centuries enormous changes took place in the economic life of Europe and most especially in England. Capitalism became well established, but there was no coherent theory to justify it. The ethical framework of medieval economics came under attack, but there was little to replace it. Or rather, what sought to replace it was a new concept which preached quite openly that “greed is good.” This idea was most famously expressed in Bernard Mandeville’s *Fable*

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<sup>17</sup> Amintore Fanfani, Catholicism, Protestantism, and Capitalism (Norfolk, Virginia: IHS Press, 2003) 59.

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<sup>18</sup> Hirschfeld, *Standard of Living and Economic Virtue*.

of the Bees: or Private Vices, Publick Benefits (1724) “in which he put forth the seemingly strange paradox that the vices most despised in the older moral code... would result in the greatest public good.”<sup>19</sup> Further, we see a complete reversal of Aristotle’s distinction between natural and unnatural exchange. Whereas natural exchange aimed at providing the goods necessary to live, for which money was merely a means and not an end, the *summum bonum* of the new ethic was the unlimited earning of money for its own sake.<sup>20</sup>

Into this ethical vacuum came the sages of the Enlightenment. If the older sages made economics a colony of ethics, the divines of the Enlightenment reversed that order. The problem of the Enlightenment was to root all explanations in some naturalistic principle, be it logic or human psychology or induction based on observations of nature; the authority of religion and philosophy was no longer to be trusted. Therefore, “natural law” could be the only sure guide through the sectarian and partisan maze. God would be known not through written revelation, but through the revelation of nature. Thus, the economist served a dual role: he interpreted the economic stars to man and read therein the will of God. God, or nature, was still invoked as a final cause, but he always operated through secondary causes. These secondary causes could be known “scientifically”

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<sup>19</sup> E. K. Hunt, History of Economic Thought: A Critical Perspective (Armonk, New York and London, England: M. E. Sharpe, 2002) 33.

<sup>20</sup> Max Weber, The Protestant Ethic and the Spirit of Capitalism, trans. Talcott Parsons, 2nd Roxbury ed. (Los Angeles: Roxbury Publishing Co., 1998) 53.

without any written revelation from the deity god-nature.<sup>21</sup> The major role of the “priests” of this god-nature was to answer the question raised by Mandeville: “How do ‘private vices’ become ‘publick benefits’?” Without any conscious appeal to the common good, how could the common good result? For most of the classical and neoclassical economists, the market becomes a theodicy in which god or nature is a Machiavellian sovereign who weaves long term benefits from purely private interests.<sup>22</sup> But as “nature and nature’s God” are more thoroughly “understood,” God himself becomes less necessary and nature becomes all we need to know. Thus the economist replaces the preacher and the philosopher. The “laws” of nature, interpreted by Enlightenment divines, become the hand of God in human affairs, and economics is raised to the level of ethics, if not actually surpassing them. The transitional figure in this process is Adam Smith (1723-1790). There were, of course, Enlightenment treatises on economics before Smith, but by popular acclaim he is regarded as the founder of “classical” economics.

#### ADAM SMITH

Smith was a professor of moral philosophy at the University of Glasgow and was part of the Scottish Enlightenment. He was a Stoic philosopher and not a particular fan of Christianity. But he was a bitter enemy of the mercantilist class and a friend to the working classes. Smith’s real aim was

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<sup>21</sup> John Milbank, Theology and Social Theory: Beyond Secular Reason (Oxford: Blackwell Publishers, 1990) 39.

<sup>22</sup> Milbank, Theology and Social Theory 37.

to do for political economy what Newton had done for astronomy: reduce the seemingly endless complexity to a simple natural rule. As Newton had “tamed” gravity with the inverse square law, Smith hoped to find a similar law for political economy.<sup>23</sup> The problem was, however, that Smith found not one, but two “Newtonian” principles: The Labor Theory of Value and the “Invisible Hand” theory, and they were opposed to each other; one theory emphasizes conflict and the other emphasizes harmony.<sup>24</sup> Hence Smith becomes an iconic figure to two opposed economic philosophies, capitalism and communism. In the invisible hand theory we have the foreshadowing of what will become “neoclassicism.” But from the Labor Theory of Value is born Marx’s theory of capitalism.<sup>25</sup>

The Labor Theory is actually a theory of production and hence an inherently “distributive” theory. The “invisible hand,” on the other hand, is a theory of exchange and hence a theory of corrective justice. Smith was not able to unite the halves of his theory into a single theory. There is even a different rhetoric that surrounds both theories. When speaking of the Labor Theory, Smith is as vitriolic as any Socialist agitator could hope to be. For example, he tells us that the merchant class is in a constant conspiracy against the public interest: “People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against

the public, or in some contrivance to raise prices.<sup>26</sup> Yet when Smith speaks of the invisible hand, this same merchant-conspirator becomes a public benefactor who, in pursuing his self-interest,

... intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it.<sup>27</sup>

Commentators have frequently noted the apparent schizophrenia in *The Wealth of Nations*. The real problem is that Smith is dealing with two halves of a proper economic theory, but he cannot put them together. In the century following Smith, economic theory bifurcated into two distinct traditions, the Labor Theorists and the Utilitarians. The Labor Theorists include Ricardo, Hodgskin, Mill (sometimes), and Marx. In the Utilitarian tradition, we find Say, Senior, Mill (sometimes), and Bastiát. For a century, they glowered at each other and engaged in some rhetorical excesses against each other, but neither side had a consistent theory of wages and prices, or described accurately the workings of the economy. This is not surprising, since both sides worked with only half of the necessary theory; their theories are *either* distributive *or* corrective, but never both. These economic fragments make war on each other, a war that neither can win.

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<sup>23</sup> John D. Mueller, *God and Money* (Washington D. C.: ISI Books, Forthcoming, 2006) 49.

<sup>24</sup> Hunt, *History of Economic Thought* 45.

<sup>25</sup> Mueller, *God and Money* 62.

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<sup>26</sup> Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (Amherst, New York: Prometheus Books, 1991) 137.

<sup>27</sup> Smith, *The Wealth of Nations* 351-2.

*THE TRIUMPH OF "NATURAL LAW"*

If justice is the basis of economics, then any economic theory that does not encompass both the corrective and distributive functions of justice is an incomplete theory. Neither of the schools of classical economics—Labor Theorists or Utilitarians—provides a complete economic theory. Later theorists recognized the incompleteness and tried to correct it, not by enlarging the theories to include both aspects of justice, but by mooted questions of justice altogether. They sought a natural law, one as inviolable as the law of gravity, and one therefore unrelated to considerations of moral agency. The law they choose for their theorizing was that of *marginal utility*. The price of any commodity, including the commodity known as labor, is derived neither from its labor content nor from its total utility; rather, the price is based on the marginal utility, the usefulness of each additional increment. On this foundation, marginalists of the 19<sup>th</sup> century such as Menger, Marshall, Walras, Jevons, and Clark were able to build models of partial and total equilibrium that referenced not justice but differential calculus. By working through an invariable “scientific” principle, the marginalist revolution mooted earlier questions of justice. The moral order, which had heretofore been the foundation of the natural law, was now banished to a separate and indistinct realm.

Nor was the moral law worse off for this change, at least theoretically, since the models promised exactly those things that the “just price” theory had promised: an economy in equilibrium without excess profit or economic rents, with both labor and capital fairly

compensated, and compensated by laws that anyone with the requisite training could inspect. The operation of the free market would drive prices to costs thereby eliminating any opportunity for exploitation. Incomes, whether from rents, profits, or wages, would be normalized to each other and there would be no vast differences in wealth and poverty. It is a vision that Aquinas could endorse, but without Aquinas’s mechanism of the just wage. Natural law would succeed in economics as it had in astronomy and physics; just as in the case of Galileo, the authority of the theologians would be replaced by the authority of the scientists. Calculus would triumph were morality had failed. The mistake in both cases was thought to be the same: By concentrating on the meaning of the heavens, the priests had missed the motions of the stars; so too in economics, by concentrating on justice, they had missed the motions of money. It would be unfair to say that the marginalists wanted to do away with justice; rather, they wanted to rationalize it, to reduce it to some law, a law that could say what was just in every situation with a calculation that would be more certain than the pronouncements of the priests.

Still, the priests weren’t giving up. While the marginalist revolution was taking place, the chief priest of the Roman Church, Leo XIII, was writing his scandalous encyclical, *Rerum Novarum*. It was scandalous because, in the face of overwhelming scientific consensus, he insisted on a purely moral concept, the just wage. The Pope did not bother to relate this wage to the productivity of the worker, but rather to the worker’s needs, and especially to the need to support his family and save a little besides. But as far as the marginalists were concerned, the

Pope could rail against the system all he wished, but he couldn't change the numbers. The mathematics were certain and that was that. Or so it seemed.

*THE BIFURCATION OF JUSTICE AND ECONOMICS*

Although the marginalist theory promised equity and equilibrium, fairness and stability, the actual results were otherwise. Capitalism became an increasingly unstable system subject to ever more violent cycles of economic euphoria and depression. The gap between rich and poor increased, adding to the overall sense of unfairness. Clearly, something was wrong with the theory. In the midst of the crisis of the Great Depression, John Maynard Keynes (1883-1946) came up not just with an explanation for the crises, but with policy prescriptions that have become embedded, for better or worse, in the policies of every single developed country. Although Keynes is often considered a radical, the truth is that he accepted the neoclassical model nearly without change:

Our criticism of the accepted classical theory of economics has consisted not so much in finding logical flaws in its analysis as in pointing out that its tacit assumptions are seldom or never satisfied, with the result that it cannot solve the economic problems of the actual world.<sup>28</sup>

Keynes's primary insight was that in the face of vast inequalities, full employment equilibrium is impossible. Keynes locates the primary failure of

neoclassicism: "The outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes."<sup>29</sup> Keynes's ultimate goals were greater than making minor adjustments during depressions; his real interest was in distributive justice, not just from the moral perspective, but from the view of practical economics. The remedy for the business cycle "would lie in various measures to increase the propensity to consume by the redistribution of incomes..."<sup>30</sup> His point was that vast differences in wealth and poverty are themselves the cause of unemployment and depressions. This was based on the practical and undeniable proposition that the wealthy have a lower marginal propensity to consume than do the poor.<sup>31</sup> Thus, as wealth is concentrated, purchasing power is lost to the economy, and with this loss comes the loss of employment.

Keynes thus reintroduced the lost question of distributive justice. However, justice has a peculiar quality in Keynes: It is no longer distributive, but *re*-distributive. The question becomes completely politicized: The economic system produces the wealth and the politicians tax and redistribute it. Justice is no longer an intrinsic fact of the economic system, but a "correction" to it made by the political system. Justice and economics are now totally bifurcated, each in their separate realms. There is certainly some warrant for this in traditional discussions of justice. In

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<sup>28</sup> John Maynard Keynes, *The General Theory of Employment, Interest, and Money* (San Diego, New York, London: Harcourt, Inc., 1964) 378. What Keynes refers to as "classical" theories, we now label "neoclassical."

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<sup>29</sup> Keynes, *The General Theory* 372.

<sup>30</sup> Keynes, *The General Theory* 324.

<sup>31</sup> Keynes, *The General Theory* 31.

Aristotle, for example, merit seems to be determined politically, “for democrats identify it with the status of freeman, supporters of oligarchy with wealth (or with noble birth), and supporters of aristocracy with excellence” (*Ethics*, 1131a, 25-29). However, this is a superficial reading of Aristotle, since he did not draw sharp distinctions between the political and the other orders; the *polis* was the locus of all social interactions and hence is more closely identified with culture broadly conceived rather than with a narrow conception of politics.

Nevertheless, the re-introduction of distributive justice, in whatever form, worked to modify the cataclysmic effects of capitalism. The business cycles have been rendered milder, and the distribution of wealth has become more equitable. However, there are some problems. Income redistribution will always require a vast and intrusive government bureaucracy to collect and disperse the funds. In the process, each person becomes a mere client of the state rather than a true citizen; where subsidies are to be given or funds paid, the idea of a common good, so crucial to Keynesian analysis, dissolves into a war of economic interests. Further, there is the serious question of whether Keynesian policies can be maintained in the face of mounting debts. These debts are not a necessary part of Keynes’s prescriptions, because in theory the debts built up in bad times are to be repaid in good times. But such debts may be a practical consequence, since it is politically easier for governments to incur debts than to repay them. The age of Keynes may be coming to a close simply because we can no longer afford it. But what can possibly replace it without returning us to the days of

economic turmoil and misery? There can be little doubt that in an age of war, communism, fascism, and turmoil, Keynes saved capitalism for the capitalists. The question now is whether capitalism can be saved from Keynes.

Of course, there would never have been a need for Keynes had marginalist theories worked as advertised. Clearly, there is some fault in the system that needs to be addressed. Our next task, then, is to analyze marginal utility theory, and particularly marginal productivity, to see where the fault lies. Our question is, “Why does a theory that claims to represent ‘natural law’ behave so unnaturally?”

### **MARGINAL PRODUCTIVITY**

#### *J. B. CLARK AND THE DISTRIBUTION OF INCOMES*

Marginal productivity is based on the intuitively obvious “law of diminishing returns.” It is well understood that only so many workers can be set to work on a given process before their output starts to decline. For example, let’s say one worker in a strawberry field can pick ten boxes in an hour and that this rate can be constant for the first ten workers hired. But at some point, the additional output (that is, the “marginal product”) from the last man hired will decline; the additional workers will just start getting in each others way. Let us say that the output declines to six boxes/hour for the eleventh man, three boxes/hour for the twelfth, one for the thirteenth and none for the fourteenth; the fifteenth picker will actually decrease the overall output by some amount. If the pickers are paid the equivalent of three boxes/hour, then it makes no sense to hire the thirteenth man; his wage would exceed the value of

what he could add to production. The law of marginal productivity states that *all* of the pickers will be paid only what the last man that can be hired is paid, or in this case the equivalent of three boxes of strawberries/hour.<sup>32</sup>

This was explicit in all of the theorists of the marginalist revolution, but John Bates Clark attempted to show that it was not only a scientific “fact,” but that it revealed the very workings of the moral order; workers are paid the marginal product because that is all they deserve. While wages might *appear* to be based on the free bargaining of the free market, they are in fact based on “a deep acting natural law” which dictates the outcomes for these “free bargains.”<sup>33</sup>

*Where natural laws have their way, the share of income that attaches to any productive function is gauged by the actual product of [that function]. In other words, free competition tends to give labor what labor creates, to capitalists what capitalists create, and to entrepreneurs what the coordinating function creates.*<sup>34</sup>

The task for Clark was then to show that the marginal wage, the wage of the least productive person (or as Clark termed him, the “marginal man”<sup>35</sup>) represented the “specific product of labor,” and of labor alone. His strategy was to start with the law of rents. As Ricardo noted that the least productive land commands no rent, Clark reasoned that the least productive

tools and machinery also commanded no rents. Thus, workers could keep all the income they could get from such marginal tools. This amount corresponds to the marginal rate for labor and is its natural wage.<sup>36</sup> How was this wage correlated to the “specific product of labor”? Clark argued that it was possible to fix the specific amounts of production that were separately attributable to capital and labor.<sup>37</sup> If the product of the one could be fixed, then the product of the other would be the remainder, (Clark only allowed for two factors of production, labor and capital, with land being just another kind of capital.)<sup>38</sup> To fix the portion of the product attributable to labor alone, Clark reasoned that the “marginal man” could be hired “with no change in the amount or character of capital goods.”<sup>39</sup> Therefore, the amount he added to production—and this amount alone—was the only part of production attributable to labor alone and constituted the “specific product of labor.” Labor was therefore entitled by “natural law” only to this part of the produce. Clark made no attempt to fix the “specific product of capital”; he merely assumed it was the whole product minus the wages.<sup>40</sup>

Clark believed that the forces of free competition would force prices to equal the cost of production,<sup>41</sup> driving the rate of profit to zero, so that the entrepreneur would earn little more than

<sup>32</sup> Bradley R. Schiller, Essentials of Economics, Second ed. (New York: The McGraw-Hill Companies, 1996) 172.

<sup>33</sup> John Bates Clark, The Distribution of Wealth: A Theory of Wages, Interest, and Profits (New York: Augustus M. Kelly, 1899) 2.

<sup>34</sup> Clark, The Distribution of Wealth 3.

<sup>35</sup> Clark, The Distribution of Wealth 94.

<sup>36</sup> Clark, The Distribution of Wealth 97.

<sup>37</sup> Clark, The Distribution of Wealth 47.

<sup>38</sup> Clark, The Distribution of Wealth 190.

<sup>39</sup> Clark, The Distribution of Wealth 101.

<sup>40</sup> Clark, The Distribution of Wealth 195.

<sup>41</sup> Clark, The Distribution of Wealth 16.

the worker.<sup>42</sup> This introduces a conundrum into the theory: the whole system depends on the entrepreneur who seeks a profit, yet, to the degree that the theory works at all, no profit is possible.<sup>43</sup>

Since Clark had relied so heavily on the Law of Rents to determine the “natural” distribution of incomes, it was necessary to show that all income—whether from land, labor or capital—is a form of rent. Clark argued that since wages are a “differential gain” they were the same as ground rent. From this stunning non-sequitur, Clark concludes: “It is one of the most striking of economic facts that the income of all labor, on the one hand, and that of all capital, on the other, should be thus entirely akin to ground rent.”<sup>44</sup> Why the effort to equate all incomes with ground rent? Ground rent is rent paid for the ground that stands beneath any productive asset. The problem with ground rent is that it has no economic function and hence represents a pure *economic rent*. Economic rent is an amount paid to a factor of production over and above that which is necessary to keep it in production; it is the very measure of economic inefficiency. But land has neither production cost nor depreciation cost. Thus the entire amount paid for such rent is economically and morally suspicious. No one claims that the landowner, merely by virtue of owning the land, adds any value to it; indeed, it is not contentious to point out that his title adds nothing productive to the land. The landowner’s claim to all but the

marginal product is a purely legal one, and neither a moral one nor an economic one. It is based solely on the monopoly status that land and the landlord enjoy.

The reduction of all incomes to rent also served a practical purpose: Since all incomes are from the same source, they can be treated by the same mathematics. To accomplish this feat, Clark disembodied capital goods to treat them as a more abstract “capital” with no fixed content. Clark performed the same courtesy for labor. He argued that labor is a “permanent” force<sup>45</sup> apart from any individual laborer.<sup>46</sup> This disembodiment of labor and capital was the last bit of the theory necessary to unite all factors of production under the mathematics of the Law of Rents. In classical economics, it was necessary to have different explanations for the different forms of income; the Law of Rents for land, the Labor Theory of Value for labor, and some sort of surplus value theory for profits. But now all three of these factors, in their disembodied states, could just be interchangeable “x’s” in a production function solvable by differential equations.

#### ARISTOTLE OVERTHROWN

Clark believed that in the workings of marginal productivity he had discovered the workings of God himself. He published in purely religious journals claiming to have worked out the laws of the moral order, “natural laws” which was merely the working of God’s plan and which would eventually lead to the New Jerusalem, the kingdom of God

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<sup>42</sup> Clark, The Distribution of Wealth 111-2.

<sup>43</sup> Hunt, History of Economic Thought 306.

<sup>44</sup> Clark, The Distribution of Wealth 191.

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<sup>45</sup> Clark, The Distribution of Wealth 157.

<sup>46</sup> Clark, The Distribution of Wealth 158-9.

on Earth.<sup>47</sup> But this would happen in a deterministic fashion, under the auspices of a mechanistic God. There was little room for any human or divine intentionality as the whole system operated completely on “auto-pilot.” It is therefore the supreme irony that Clark’s implicit view of history was no different from that of Hegel or Marx.

Nevertheless, if Clark’s claims are correct, then his is a remarkable achievement. All of economics, and all of justice as well, are reduced to the “science” of exchanges, that is, to corrective justice. Aristotle’s claim that distributive justice has an irreducible cultural element would be false and economics would be a completely self-contained science that is entirely free of moral, historical, or cultural elements. If Clark is correct, then Aristotle must be wrong. Any attempt to introduce normative considerations into economics would be, at best, counter-productive and, at worst, anti-scientific.

### **THE CRITIQUE OF MARGINAL PRODUCTIVITY**

#### *THE REALITY CHECK*

The theory of marginal productivity claims that in economies where the wages are at subsistence levels we will see full employment, a high rate of labor force participation, little difference between the very rich and the very poor, and a full utilization of all economic resources. Conversely, in high wage states we would expect to see low labor force participation, high unemployment, under-utilized economic

assets, and high differentials between wealth and poverty. Yet, when we look at the real world, we find precisely the opposite, and we find this in nearly every single case. Now, in any single case there may be any number of *ad hoc* explanations for the divergence of actual results from the theoretical ones. However, when every single case seems to require an *ad hoc* explanation, we may begin to suspect that there is something wrong with the theory itself, no matter how logically consistent it may appear to be.<sup>48</sup> Logic, after all, is only a test of validity and not directly a test of truth. We have seen that Keynes’s prescriptions were necessary to correct the imbalances which, according to marginalist theory, should not exist. Why then is marginal theory untenable in real economies?

#### *THE NECESSARY CONDITIONS*

One critique of marginal productivity is conceded by all sides in the debate: The theory requires a long list of conditions to be fulfilled that cannot in fact be fulfilled. Some of these include perfect competition, constant returns to scale, full employment of resources, etc. Perfect competition, for example, is impossible even at a theoretical level because there are always barriers to market entry, aside even from the barriers created by market power and government action. Further, this assumption presupposes a large number of small firms such that none of them has much power to influence the market price to any great extent. But many industries are in fact composed of a small number of large firms with

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<sup>47</sup> Robert H. Nelson, *Economics as Religion: From Samuelson to Chicago and Beyond* (University Park, Pennsylvania: The Pennsylvania State University Press, 2001) 102.

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<sup>48</sup> Lawrence A. Boland, *The Principles of Economics: Some Lies My Teachers Told Me* (London and New York: Routledge, 1992) 206.

tremendous market power. As Paul Ormerod points out,

By definition, any model necessarily abstracts from and simplifies reality. But the model of competitive equilibrium is a travesty of reality. The world does not consist, for example, of an enormous number of small firms, none of which has any degree of control over the market in which it is operating. Small firms may be fashionable at present, but it is large multi-national companies... which dominate the world economy. It is entirely illegitimate to make the link between the model and the observed success of the Western market economies.<sup>49</sup>

In short, marginalist theory models a business system that does not, in fact, exist.

#### EMPIRICAL VERIFICATION

An even more serious critique is the fact that marginal productivity is an empirical theory that simply does not permit of empirical verification. For all of its theoretical power, marginal productivity is not actually used by businesses, which is suspicious. The example of the berry-pickers previously given seems to be so obvious—to economists—that it needs no verification. But a *businessman* will immediately spot the fallacy. If an entrepreneur has 10 workers in the field, it is highly unlikely that he has ten pickers. That is, he does not have a *homogenous* workforce as the theory presumes. Rather, he might have eight pickers and two supervisors, or one supervisor, seven pickers, and two performing a collection function, or some other configuration of labor. For a

process that is losing money, the question becomes, “Who is the ‘marginal man?’” Are there too many supervisors, or too few? Too many collectors, or too few? Too many pickers, or too few? Marginal productivity cannot answer these questions, cannot be computed, and therefore can give the businessman or woman no useful information.

We could of course force a homogenization of labor on the formula by divorcing the work from the worker and reducing everything to some unit, let us say the wage of the lowest paid worker. So if our ten workers are divided into seven pickers (the lowest wage), one supervisor (who makes half as much again as the pickers, or 1.5 picker-units), and two collectors who make 25% more than the pickers (or 2.5 picker-units), we would have a total of 11 picker-units. Now we have a number to plug into the formula, but the formula can yield no useful results, just as before. If we find that our picking operation is losing money, then we can run our productivity formula and discover, let us say, that we are 2 picker-units past our point of marginal productivity. But which two units? Do we have too much or too little supervision, collection, or picking? We are left with exactly the same questions as before, and exactly the same lack of answers.

It comes therefore as no surprise that attempts to verify marginal productivity empirically have proven a failure.<sup>50</sup> As Garrick Small notes of marginal analysis in general:

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<sup>50</sup> Anwar Shaikh, "Laws of Production and Laws of Algebra: Humbug Ii," *Growth, Profits and Property*, ed. Edward J. Nell (Cambridge: Cambridge University Press, 1980).

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<sup>49</sup> Paul Ormerod, *The Death of Economics* (New York: John Wiley & Sons, Inc., 1994) 48.

Some economists therefore have suggested that prices can sometimes be shown to behave *as though* firms were performing marginal analysis, even though it is known that they do not. ... Apart from looking a lot like Ptolemaic astronomy, actual prices cannot be shown to be capable of being reliably predicted by marginalist methods because of the practical impossibility of generating the mathematical relationships with anything like the precision necessary to yield a specific price.<sup>51</sup>

### THE SOCIAL NATURE OF PRODUCTION

The reason the individual factors of production cannot be computed has to do with the assumptions of the marginal productivity theory, assumptions which are hidden in most accounts but which Clark, at least, attempted to make explicit. Clark was searching for the amount that labor “separately” produced. He assumed that the “marginal man” could be added without any addition of capital and therefore represented “empty-handed labor.”<sup>52</sup> This is empirically false. The marginal man is not added without an addition to capital; at the very least there is the capital represented by his wage, and he can produce nothing without consuming some capital in the form of tools and materials.

Clark did not actually attempt to compute the “separate product of capital” as he did for labor. Had he attempted to do so he would have

discovered that the separate product of capital— or of labor— is the only precisely known number in all of economics; it is precisely zero. Take some item of capital, say a truck, and watch it all day with a careful eye to see what values it produces. There will be exactly none, unless and until a driver mounts the cab to make some deliveries. Take a pot of capital, let's say some cash, and fertilize it and water it with all the care you can. It will still refuse to grow. Unless and until someone takes the money out of the pot to purchase tools, materials, and the labor to work them, it will not produce any values. All production is *social*; it is the intersection of land, labor, and capital, and nothing happens independently; hence, there can be no “specific” or “independent” theories of production. The same rule applies to labor. “Empty-handed labor” is simply another name for “unemployment”; without capital, labor can produce nothing. The factors of production— land and labor— do not, in themselves, have a marginal product; only the process as a whole does. One particular arrangement of supervisors, collectors, and pickers will have a different marginal productivity than another arrangement, and it is only these various arrangements that can be compared. Marginal productivity for a given factor cannot be computed because it does not exist.

Therefore, management must use its best judgment in allocating the rewards in a way that best utilizes the company's resources and best encourages the contribution of the workers. There is no “natural” division of the product; it is a matter of distributive justice and, as Aristotle pointed out 2,500 years ago, distributive justice follows no “natural” rule, but will

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<sup>51</sup> Garrick Small, An Aristotelian Construction of the Social Economy of Land (Sydney, Australia: University of Technology, Sydney, Australia, 2000) 159.

<sup>52</sup> Clark, The Distribution of Wealth 171.

always involve a cultural decision. Contribution to the production process is computed by merit, but merit will involve a judgment on the part of management, a judgment that can be reduced to no set formula.

#### *TWO FACTORS OR THREE? OR ONE?*

The marginalist revolution reduced the three factors of production found in classical economics to two, labor and capital; land simply disappeared from economic theory and became another form of "capital." Clark carried the process further by eliminating labor and treating it as just another "bit" of the capital fund. This made the mathematics much simpler. But alas, it allowed for a clean break with reality. Land and capital are not identical and obey different economic laws. And labor is different from land and capital in ways too obvious to mention.

Marginal productivity might work very well for man-made things, at least in some circumstances. If the price of widgets is high enough to collect an economic rent, then widgets will attract capital and entrepreneurs, the supply will be increased and the price lowered. If the price is too low to pay for production costs and depreciation, producers will exit the market, lowering the supply and raising the price. Thus, the promise of marginal productivity is an economy free of economic rents with great equity and full employment. After all, equity equals equilibrium; they are practically the same word and very nearly the same thing. And economic rent is the enemy of both words. But the theory breaks down for land and labor. Since you can't manufacture land, no one can undercut the market and hence marginal productivity will not apply; land, having no production or

depreciation costs, will always earn a pure rent. As for labor, it cannot be withdrawn from the market when the price does not cover production costs (the family) and depreciation (sickness and old age.) Hence, marginal productivity does not fulfill the basic requirements of any economy: to provide the necessities of life to all participants. Therefore, marginal productivity cannot be a description of any reality. It describes a world where land is manufactured at will and workers, when not needed, can shut themselves off until the market improves. Hence, marginal productivity does not even rise to the level of good science fiction.

#### *THE DEFINITION OF CAPITAL*

As badly as marginal productivity works for labor, it does even worse at describing the productivity of capital. The marginalists have to aggregate capital into some common number in order to use it in the marginal productivity formula. But quite obviously, buildings and trucks and machinery are all different things and have different rates of return. So what number should we use to plug into the formula? All too easily we answer "price!" but this doesn't work at all, because the price depends on the return. How much an asset returns is supposed to be based on its marginal productivity, just as the wage is. But this turns out to be circular: the price depends on the productivity, but the productivity depends on the price.

Clark aggregated all capital goods into a mysterious fund called "capital," a fund that was distinct from any physical thing that was in the fund. The necessity of doing this is obvious: It is difficult to use a machine in the

formula and would be much better if one had a number. But this aggregation makes even less sense than it did in the case of labor. We need to compute the formula to know what return to use in the formula, which means we need to compute it before we compute it. The whole logical structure is now shown to be totally incoherent. As Joan Robinson noted:

We must agree (though mumpsimus will continue in the textbooks) that marginal productivity of capital in industry as a whole has been shown to be a meaningless expression. We must look somewhere else to determine the laws which regulate the distribution of the produce of the earth among the classes of the community.<sup>53</sup>

*SUMMARY: EQUITY AND EQUILIBRIUM*

We started with something that was— and is— intuitively obvious, the Law of Diminishing Returns, and tried to make it into a formula which solves all allocation, pricing, and distributive functions. At that point, the theory becomes incoherent. How could we have moved from the intuitively obvious to the patently incoherent so quickly? It is certainly true that the returns from any asset— be it land, labor, or capital— diminish as further units are added, so that at some point we cannot profitably employ an additional unit of that asset. But where does that point of marginal productivity come? It would greatly simplify the task of management if this could be known by a formula. If the marginal productivity of all factors could be known, then the proper allocation of

resources would be equally obvious to the CEO and the janitor. The preparation of the most complex budgets would be a trivial matter: Each function would state its marginal productivity and the entire budget would be a matter of a few moments work with a calculator. Executives would have even more excuse to spend their afternoons on the golf course than they already do, presuming there could be found a reason to hire executives in the first place.

Thankfully for the profession of management, the problem is not nearly that simple. Judgment— managerial judgment— is required for the proper allocation of resources and the compensation of employees. These judgments cannot be reduced to a formula. The problem is that the marginalist mathematics tried to reduce all production to exchanges and derive distributive justice formulaically from corrective justice. This cannot be done. Insofar as production is a *social process*, the distribution of rewards must be a social decision. In other words, the theory has reversed the natural order between distributive and corrective justice. Distributive justice must be prior because it deals with production, and production is prior to exchange; you must *make* something before you can *exchange* it.

In the same way, marginalist theory assumes that equity would result from the attainment of equilibrium, when in fact the reverse is true: equity is prior to equilibrium. If we examine the assumptions of the marginal productivity theory, assumptions such as a large number of small firms and perfect competition, we find that they are assumptions connected more naturally with well-distributed property. That is to

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<sup>53</sup> Joan Robinson, "The Measure of Capital: The End of the Controversy," *The Economic Journal* 81 (1971): 602.

say, it is connected with *equity*. But the theory is supposed to produce equity. Therefore, the whole theory assumes what is supposed to be its result as its starting point. The theory will have to be reconstructed, and reconstructed in the right order. That is, from distributive justice to corrective justice, from equity to equilibrium.

We can summarize our conclusions in this way: ***Since all production is a social process, we can compute a marginal product only for a process as a whole, never for a factor within that process.*** There is no “empty-handed labor” whose “productivity” can be calculated, nor any capital independent of labor that can produce any values. It is *only* the intersection of land, labor, and capital that produces economic values. This being the case, how then can we judge the relative compensations to be given to the factors of production? If marginal productivity formulas produce no useful results which can be examined by all sides, how then shall we construct a theory of compensation— that is, a distributive theory— that can be acknowledged by all parties to the production process?

### THE JUST WAGE

#### NATURAL LAW AND PROPERTY

The neoclassical economists attempt to build a system based on natural law, but their concept of natural law is at odds with traditional Christian thinking on the subject. The Christian idea of natural law views the law in light of the meaning and purpose of things, their *teleology*. Thus an economy cannot be merely the operation of “automatic” laws that have no necessary relation to the objective needs of human beings and

their social situations, but is something subordinated to the ends and purposes of persons and societies.<sup>54</sup> The perception of these ends and purposes will vary from culture to culture, but we can nevertheless detect some common threads: the necessity of providing for all citizens, the necessity of providing some rules of exchange, the necessity of providing for the next generation, and so forth. But the most primary economic question that a culture must deal with is the question of property. The claims to some portion of the output of production are claims of property rights. Yet, very little attention is given to examining the basis of property rights so that in effect the whole theory rests on unexamined and non-economic assumptions. Property is taken as a given or self-evident assumption, but is it? In fact, the system of allodial property which we regard as “natural” is in fact a social convention of relatively recent origin and that many other property systems have existed and do exist.

Property rights are made up of two considerations: ownership and use, with the former subordinated to the latter, at least to some degree. For St Thomas, the common use of property was part of the natural law, while the private ownership was a social convention, valid to the degree that it helps us to bring forth the goods of the earth and make them widely available. (*ST* II-II, 66, 3) Thus while property is conventional in itself, it can be used to

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<sup>54</sup> Of course, the Enlightenment idea of natural law is modeled on physics or astronomy. It is certainly true that we study the movement of the stars without any explicit reference to the moral order. However, the idea that men are moved in the same way as the stars is more akin to astrology than to astronomy.

serve the purposes of the natural law. However, there is at least one form of property that is completely natural.

#### NATURAL PROPERTY

When we look at property, we can note that each person has a property in himself. This constitutes a “natural” property as it is self-evident and reducible to nothing else. Furthermore, each person has a natural title in his labor and to what his labor produces. A person who makes something is considered the owner of that thing, to the extent that the labor and the materials are his. Of course, people make most things in cooperation with others, so that the product is a social product, and hence no one person can claim the whole output, but only what is proportional to his contribution. This right to a proportional share is based on the fact that to produce something a person must contribute a portion of his life, his natural property, and he therefore has a just claim to support for that portion of his life, his own property, which he has contributed to the product.<sup>55</sup> This leaves unanswered the question of the *level* of support, whether we will make of the worker a prince or a pauper, but unquestionably establishes a right to some level of support.

In producing anything, however, each person or each firm also makes use of two other factors: previously man-made things (capital) and land, which includes the raw materials that land supplies. How are these other factors to be compensated? Note that we are dealing with *three* factors of production, land, labor and capital, rather than just

*two*, labor and capital, as in Clark. Land is a gift of nature and labor the gift of the worker. But what about capital? Capital itself regresses to land and labor (and to previous capital, which regresses to land and labor), so that if we sort out the compensation between land and labor, we can also determine capital’s compensation.

#### CONVENTIONAL PROPERTY

We discussed labor’s compensation as based on the portion of his life that a laborer contributes to the final product. But what contribution does the landowner make? In the first place, we note that the landlord makes neither the land nor the raw materials which can be extracted from it. His claim is a legal one, based on whatever operations of title prevail in his society, that is to say, on purely social conventions. So how does the landowner come into possession of the land, and what is the nature of his title? Almost all theorists, from John Locke to John Paul, agree that land was originally meant for common use and given to all; it is taken out of common usage by some variant of the labor theory of value. For John Locke, this strips land of all communal values, but for Aristotle, Aquinas, and John Paul II, land can *never* lose its social values. The privatization of land is justified on pragmatic grounds alone, namely that this best serves the common good. Since the justification is only pragmatic and not “natural,” it fails when land ownership no longer advances the common good. But whatever view of land one takes, what is obvious is that it arises not from natural law, but from social convention and positive law. Thus the compensation given to land is fixed socially, not “naturally.”

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<sup>55</sup> Small, The Social Economy of Land 242.

If all values from land are “privatized,” then the landlord will be able in principle to extract all marginal values and the Law of Rents will hold. But the entire structure of private ownership rests on convention and not on economic law; different conventions will yield different results. These conventions, whichever ones a society chooses, will rest on moral considerations entirely. It may be the morality of the jungle where the strong prey on the weak in the name of pure self-interest, or it may be based on some vision of the common good and the natural right of people to the true products of their labor. The task of the social scientist here is not to arbitrate among these visions and pronounce an “economic” decision, but to compare the likely results of various social conventions using both theory and history as a guide.

#### SUBSISTENCE

Several points flow from the discussion so far:

1. The worker has a *natural* right to the values produced proportional to the share of his life that he surrenders to the production process.
2. The capitalist has the same rights proportional to his labor and to the capital he supplies, which regresses to prior labor.
3. The share of the landowner is set by social convention with a view towards the legitimate needs of the landowner and the common good. His right is not natural because he surrenders no portion of his life to supply land and raw materials, but is based solely on social conventions.

The question now becomes, “How can we place a monetary value on the natural property the worker has in the final product?” The answer is rooted in the share of his life that the worker surrenders to make the product. It would seem to have three parts: subsistence; a premium for training, skills, and responsibility; and something left over for savings to acquire one’s own property and provide for one’s own security in time of need.

Subsistence would seem to be the most “objective” of the three, but it turns out to be a slippery concept indeed. This is because humans have an amazing capacity for enduring hardships. Since survival is necessary, people are not free to withdraw their labor as conditions worsen. Therefore, they will continue to bid jobs down to the level of their daily bread if they have no other options. The free market is therefore not a very good guide to subsistence levels, since it tends to arbitrate power relationships rather than economic values; when power resides mainly with the employer, the market will not only drive wages towards subsistence, but also drive subsistence itself to ever-lower levels. Further, subsistence has to be measured not just from the standpoint of the worker, but from the standpoint of his family. This is because the economy of exchange in any sane society will include support for the economy of use; it will include support for what Ivan Illich calls the right to “useful unemployment,” that is, for people who produce use values outside of the exchange economy.<sup>56</sup>

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<sup>56</sup> Ivan Illich, *The Right to Useful Unemployment and Its Professional Enemies* (London: Marion Boyars, 1978).

Useful unemployment includes, pre-eminently, the domestic arts of the household. This is not just a moral and social issue, but an economic one as well. In many areas, such as child rearing, production for use is more economically efficient than production for exchange. Exchange systems impose an entry cost of their own. For example, mothers who enter the workforce often find that increased expenses for wardrobe, child-care, transportation, meal preparation, and house cleaning often consume so much of their incomes that the benefits from their marginally calculated wages are marginal indeed. Another example of useful unemployment is education, something that adds to the productive stock of society. The best of example of useful unemployment might be childhood itself, which should be free of undue burdens of work.

Regarding labor premiums for skills and responsibilities, the market seems to do well when these are correlated to scarcity, but otherwise not so well. Of course, many jobs will get much better than subsistence because of the political power of the groups involved or because of scarcity premiums; political power can come from unions or from laws which set wages, such as a minimum wage. Or the power may come from a particular position one has, as in the case of CEOs and senior executives working with overly compliant boards of directors.<sup>57</sup> Scarcity premiums are normally related to the cost of training or to some special talent that a worker has. It is important to note here that it is *not*, as generally

supposed, the training itself or increased productivity that confers the higher wage, but solely the scarcity premium. This principle is evident when we look at two specific cases, software engineers and seamstresses. In the case of the programmers, the training required kept the numbers scarce for a long time so that engineers could easily command \$40-\$50/hour. However, as the skills have become more general, and as their own work at building the internet has made off-shoring more possible, the work is being outsourced to Indian programmers working for \$10/hour. A seamstress is also a highly skilled job; however, it is a skill that is routinely taught to nearly half the world's population from the time they are young girls. Hence, the supply is nearly infinite relative to the demand, and their skill commands no more than starvation wages. Clearly, it is the scarcity, and not the skill, that commands a premium.

Finally, there is the difficulty of determining a "savings premium." However, this might be tied to the rate needed to insure a decent retirement.

The problem then is to determine wage levels in accordance with the dignity of the worker and his family. There is a certain minimal standard that each society establishes and which constitutes for that society a "dignified" existence. This varies widely from culture to culture, but is nevertheless knowable for any given culture. This means that there is a cultural aspect which is irreducible. The problem here is that a culture can set the bar too high or too low. How much do we really need in the way of clothing? What constitutes a decent home? Do we need a television? Or two? Cable? A computer? A certain number of trips to

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<sup>57</sup> John C. Bogle, *The Battle for the Soul of Capitalism* (New Haven & London: Yale University Press, 2005).

the movies? An argument can be made that a minimal participation in our culture requires at least some of these things. But whatever the answer, there is some standard below which we regard people as being not full participants in the society.

### *MEASURING THE JUST WAGE*

But there is in fact a measure of the distance between the just wage and the prevailing wage, at least approximately and in the aggregate. This distance can be measured by the amount of transfer payments necessary to sustain demand. These transfer payments are of two types: welfare payments and consumer credit. Both of these constitute transfers of purchasing power between one group of citizens and another made in order to support demand; without these payments, there would be both a disastrous reduction in demand and a sudden implosion in the standards of society. To the extent that these things are necessary, they may serve as a proxy for the distance between social standards and actual pay. By the same token, to the extent that consumer credit exists merely to continue a cycle of pointless consumerism, it is destructive and needs to be excluded from any calculation of what a dignified life needs. Of course, some amount of consumer credit is acceptable, since it is proper to finance a long-lived item, such as a house or a car, over some portion of the life of that item. But when we end up paying next year for groceries we consumed yesterday, the situation has gotten out of hand, and all too frequently, that is what is happening; we are, too many of us, still paying for things we have consumed, discarded, or no longer care about. In any case, transfers, by subsidy or by credit, are

required to insure purchasing power in the mass of men sufficient to keep the economy going; the distance measured by these transfers is an indication of the deficiency in the just wage.

The just wage, then, is not so much a number as a criterion of judgment. We can say that the just wage is fulfilled under the following four conditions: One, that working families, as a rule, appear to live in the dignity appropriate for that society; two, that they can do so without putting wives and children to work<sup>58</sup>; three, that they have some security against periods of enforced unemployment, such as sickness, layoffs, and old age; and, four, that these conditions are accomplished without undue reliance on welfare payments and usury. While it may be difficult to give precision to any of these factors, it is certainly possible to make reasonable judgments and set reasonable standards.

### *IMPLEMENTING THE JUST WAGE*

The most potent argument against the just wage is the difficulty of implementing it. However, since we can point to hundreds of concrete examples, this difficulty is exaggerated. Here we will note just two practical implementations, the "Land to the Tiller" program of Taiwan and the Mondragón Cooperative Corporation of Spain. In the case of Taiwan, land was

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<sup>58</sup> This is not to be taken as an argument against child labor *per se*, but only against child labor in an adult context that lends itself to exploitation. Children in fact need to work, certainly inside the home and to some extent outside of it; it is part of the socialization and education process. One of the advantages of having mothers employed in the home is that they can supervise and enforce children's work.

redistributed on easy terms at below market prices from an elite class of owners to the farmers who actually worked the land. The results were dramatic. Farm production increased as farmers used more fertilizer, went to multiple cropping with as many as four crops/year, and diversified production to higher value but more labor-intensive crops. Production increased at an annual rate of 5.6% from 1953 thru 1970. The farmers suddenly had something they never had before: relatively large amounts of disposable income. This rapid increase in purchasing power among the mass of citizens fueled a rapid expansion of commerce and industry, with the result that Taiwan transformed itself from a backward society to an advanced industrial nation in only one generation, and did so with increased equality. For example, the Gini coefficient of Taiwan, measures .33; the U.S., by comparison, measures .464. The ratio in Taiwan between the earnings of the top 20% to the bottom 20% declined from 15 to one in 1950 to 5 to one by the 1970's. The current ratio for America is 14.6 to one.<sup>59</sup> Taiwan has managed 50 years of high growth rates, increased equality, and low tax rates. Unemployment was low to non-existent through most of Taiwan's post war history. Before 2000, it rarely exceeded 3% and usually was less than 2%. Since 2000, the rate has risen as high as the low 5's before dropping back to the 4% range as Taiwan struggles to adjust to outsourcing to mainland China. By human measures, Taiwan's growth was

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<sup>59</sup> Carmen DeNavas-Walk, Bernadette D. Proctor and Robert J. Mills, Income, Poverty, and Health Insurance Coverage in the United States: 2003 (Washington, D.C.: U.S. Government Printing Office, 2004) 37.

also a great success. For example, the literacy rate increased from 45% in 1946 to 93% in 1989; life expectancy went from 59 years in 1952 to 74 years in 1989 while the per capita caloric intake went from 2,078 calories to 3,070 in the same period. Living space per person went 4.6 square meters to 23.8.<sup>60</sup> Further, Taiwan and the other "Asian Tigers" were able to achieve these successes despite having population densities among the highest in the world, a fact which contradicts the prevailing dogma that population density is an impediment to growth.

A second example is the Mondragón Cooperatives. The Mondragón Cooperative Corporation (MCC) of Spain, which has a 50-year history, has proven a durable and successful firm, or rather collection of firms. One measure of its success is its sheer size: at the end of 2004, it had €18.6 billion (US\$22.3 billion) in assets, €10.5 billion (US\$12.6 billion) in sales, and 71,000 employee-owners.<sup>61</sup> The corporation manufactures appliances, electronics, car parts, and even full factories to order; it provides engineering, banking, and insurance services; it runs a university, a technical college and several training institutes; it has a retail division with markets, supermarkets, and hyper-markets. It is a major competitor in European and

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<sup>60</sup> Shirley W. Y. Kuo, "Economic Development of the Republic of China on Taiwan," Agriculture on the Road to Industrialization, ed. John W. Mellor (Baltimore: John Hopkins University Press, 1995) 334.

<sup>61</sup> Mondragón Cooperative Corporation, Most Relevant Data to 31-12-2004, 2005, Available: [www.mondragon.mcc.es/ing/magnitudes/cifras\\_i.html](http://www.mondragon.mcc.es/ing/magnitudes/cifras_i.html), August, 2005.

international markets; half of its sales are from exports. If it were an American company, its sales would place it at 154 on the Fortune 500. Thus we can safely say that the MCC, with its 50 year history, diverse product line, and large employee base, serves as a test of worker ownership.

To these examples, we may add literally thousands of employee ownership plans and cooperative ventures of every kind and size. What all of these examples have in common is that they distribute ownership of the means of production rather than merely distributing income. Where ownership is widely distributed, there is a greater tendency for the problems of income distribution to sort themselves out, as worker-owners balance their needs as workers against their needs as owners. But it is clear that there is no economic bar to a just wage; it is simply a matter of cultural values and political will. We can have a just economic order if we want one. And we can do so not by weakening economic theory, but by strengthening it, by having it take account of both distributive and corrective justice.

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