HOW WAGES ARE DETERMINED

The Effect of Interventions

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MOST PEOPLE today seem to think that producers and sellers set prices. Likewise, they seem to think that employers set wage rates. They think businessmen get rich by setting low wages for their employees and high prices for their products.

This leads many to think that employers can be compelled by law or union pressure to raise workers' wages at the expense of the owners of a business. This has been done in an increasing number of cases for a short period of time, but such wage increases cannot be maintained in the long run. Actually, it is impossible to raise every worker's wages by law or union pressure. Every law or nonmarket pressure that raises wages for some, lowers them for others.

In analyzing every economic proposal, it is necessary to examine all of its effects, not only the short-run effects, but also the long-run effects, and not only the effects on those whom the advocates seek to benefit but also the effects on those who have to pay the costs. All of these inevitable effects should be weighed before passing judgment on any attempt to interfere with free market processes.

Freedom Permits Responsible Choices

In a free market you are free to take any of many jobs open to you. Each man takes that one which, from his point of view, he considers best. When everyone is free to do this and no one is permitted to trample on the equal freedom of others to do so, when no one or no group can prevent others from taking jobs for which they and the potential employers

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reach mutually satisfactory agreements, then the Golden Rule will prevail. More workers will be producing more goods for others and everyone will have more for himself. The result will be ever-increasing production and human satisfaction. Of course, in a free market society, men will still make mistakes. But free market practices tend to reduce such mistakes by penalizing most those who make them.

We may also have a few unfortunate people who need assistance from their fellow men. For such few cases, the free market not only encourages religious and other private charities but it also provides the means with which these charitable organizations can take care of the unfortunate. So these unfortunate few do not have to become a burden on the government. We are free to act voluntarily as good Christians and take care of our neighbors who are in trouble.

In any society, in any group of men, there will also be some who will try to help themselves at the expense of others. There will be some who wish to steal, or misrepresent, or resort to force. To protect peaceful productive citizens against those who resort to such antisocial actions, governments are necessary, and very necessary.

Consumers Determine Wage Rates

There is today a popular idea that employers exploit the workers. This fallacy has been growing ever more popular since the days of Karl Marx. It was Marx's idea that employers overworked employees, paying them much less than the money values of what they produced, while keeping the difference for themselves. According to this theory, rich employers get richer and richer while the poor workers get poorer and poorer. The time would come, Marx held, when the workers would break the chains which bound them to their employers and set up a socialist utopia. According to this idea, the poor worker is helpless in a market society. He has no choice. He must take the wage that is offered to him. There is no other employer who might bid for his services.

Actually, of course, that is not so. In the absence of any social interference, workers tend to get the full value that consumers will pay for their contribution. It is the interferences by governments and the interferences by labor unions supported by public opinion, even without the strength of laws, that prevent all potential workers from getting those market values they could contribute to society.

If the idea that unions help all

workers is popular, then we are powerless to stop them from hampering the market competition. However, in an unhampered free market economy, competition tends to allocate to every factor of production, including workers, all that each contributes. It is the values that the ultimate consumers place on each particular contribution to total production that determine what businessmen can pay for that particular contribution.

The same principles apply to the wages paid for labor that apply to the sums paid for raw materials or any other factor of production.

In a free market, each employer seeks to hire as many workers as he profitably can. He hires employees up to the point at which it is no longer profitable for him to hire an additional worker because he cannot sell the product of that additional worker for the wage he must pay him. As he hires more workers, the wage rate tends to rise and as more units are produced, the market price he can get per unit tends to fall. This is the inevitable tendency of a free and unhampered market.

The more workers you hire, the higher wage rate you will have to pay. And you must pay the higher wage to all who do similar work. As you produce and offer more goods on the market, you can only sell them at lower prices. Eventually you reach the marginal point, where you make no profit on the last man you hire. Wage rates are ultimately set by the marginal productivity of labor, that is the market value added to the product produced by the marginal employee, the last man hired. This is the way the free market would work, if there were no interferences. Unfortunately, the free market is something that we have never had completely at any time and may never have. However, the nearer we get to it, the better off we shall all be.

Given the conditions which the employer faces, he must pay workers pretty much the values that consumers place on their contributions. If the employer pays a higher wage, he suffers a loss. If he does not then reduce his wage rate, his number of employees, and his production to what he can sell at a price that covers his costs, he will eventually be forced out of business. No businessman can long pay costs which he cannot get back from consumers.

In the long run it is the consumers who pay the wages. The businessman is merely a middleman. He tries to make a profit as a middleman, buying raw materials, hiring workers, and selling the products to consumers. He makes his profit, if any, by holding what he pays for the factors of production below what consumers will pay for the final product. However, once a profit appears, competitors continually bid up what must be paid for each factor of production, including labor. There is always a tendency in a free market for profits to be squeezed and disappear. This includes any profits obtained by paying workers wages lower than the market value of their contributions.

Free Competition Protects Workers

It cannot be denied that employers would always like to pay lower than the market wages. In *The Wealth of Nations,* published in 1776, Adam Smith mentioned that whenever businessmen get together they try to set wages and hold them down. However, in the free market, they are unable to do so. It is just not possible for all employers to get together and agree to hold wage rates down for any length of time. Once one employer finds he can profit by breaking such an agreement he will probably do so. If none breaks the agreement and if you have a free market society wherein anybody can become an employer, new employers will soon appear, to take advantage of the situation by offering workers more.

If the employer pays a wage lower than the market wage, that is less than the product of the worker can bring in the market, his profits will be such that he can expand his production and his number of employees. If he fails to do so and fails to raise his wage rates in doing so, he will invite new competition. In either case, market competition will raise the wage rates to the value produced by the marginal employee. And there is always a marginal employee.

In most industries there are also marginal companies. These are the companies that are just breaking even. If their costs go up a little bit, they will suffer a loss. Then they will soon be out of business because money losers cannot stay in business indefinitely.

No businessman in a free market society can long pay a worker a dollar an hour and sell his product for five dollars an hour. Why not? Because you and I and thousands of others like us would be very happy to go into that business, pay those men two dollars and sell their product for five dollars if we could. Others would soon offer to pay them three dollars, four dollars, or even four-fifty. In fact, large corporations would be very happy to make profits of just two cents an hour for every worker they employ. They are just not able to pay them much less than the market value of their product. The last one employed would not yield them any profit, particularly in a free society where anyone who thinks he sees a chance to make a profit can come in and bid away any employee who is paid less than the market value of his contribution.

The frequent refutation is, "Yes, but most people do not have the capital to start a business." Let's remember there are many savers eager to invest their money where they can earn more. If they can be shown a situation where they can earn more, they will be happy to make the needed capital available. All you need to do is to show them where a profit higher than current interest rates can be made.

Whenever there is a profit in a free market society, it attracts competition, and competition always reduces prices. This is how the market constantly allocates consumers a share of every increase or improvement in production.

Savings Raise Wages

The real secret of higher wages is increased savings per capita. Increased savings are a result of producing more than is consumed. If more goods and services are produced than consumed, then these unconsumed goods and services are available for making tools, factories, and other things needed to help increase production. American living standards have gone up over the years because generation after generation our parents have provided their children with a better start in life than their parents had. The history of our country has largely been that the first generation of immigrants provided their children with an elementary school education, the next generation saved enough to provide their children with a high school education, and the third generation sent their children through college. Now, many are going on to graduate work. In this way, each generation provided the next generation with a higher standard of living. In each case, this higher education was the result of increased savings. The earlier generations just could not afford to provide their children with what most American children now have.

When there are savings in a capitalistic system, people do not put them under a mattress. They do not dig a hole and hide them as people do in India or China where savers are afraid that if they put up a factory, the property would be seized. No, in a capitalistic society people invest their savings where they hope they will earn a return. In a capitalistic society, savings are not accumulated by the rich only. One of the great advantages of a capitalistic society is that low-income people can also invest their savings and earn a return on them. They can buy savings bonds. They can put their money in the savings banks. They can buy life insurance. Then, the banks and the life insurance companies make their savings available to businessmen and large corporations.

As a matter of fact, it is the low-income people who are the great creditors of our day. They are the ones who are hurt the most by low interest rates. It is largely the higher-income people who are debtors and who benefit from low interest rates. They are stockholders and their corporations borrow the money saved by low-income people. One of the great advantages of the free market system is that it provides a way for low-income people to participate in the earnings that savings provide.

Effect of New Savings

Savings are, of course, the only real source of old age security and higher living standards. When new savings are invested, the very first thing they do, whether they are invested in a new company or in an expansion of an old company, is to bid up wages and the prices of raw materials. They bid up everything that is needed to expand production, including labor, and you cannot make anything without labor.

Labor is one of the scarcest things in this world. There are many mines that are not mined because the available supplies of labor are worth more in other occupations. The same is true of farm lands. The same is true of every occupation. Every economic endeavor is limited by the high costs of labor. Labor is always scarce. The market allocates the scarce supplies of labor to the production of those goods and services for which consumers are expected to pay the highest prices. Other goods and services are not available because of this very shortage of labor.

With new savings, there are employers or "entrepreneurs" who are constantly trying to employ more workers. They have to bid up wage rates for the limited quantities of labor available in the market place. The factor which helps labor most is the increased savings which permit employers to bid them away from their previously lower-paying jobs. After these savings are turned into new or larger factories, they must produce goods and services previously not available.

The managers of these new expansions must determine what to produce. They try to find out what is not available that is next in importance on the value scales of consumers. They then expand the production of those things not sufficiently available that they think customers want most. They bring more production to the market. Each worker, working with more or better tools, produces more. If there has been no increase in the money supply, as more goods reach the market, the result must be lower prices. With lower prices for consumers' goods, everyone can buy more with his limited money supply. The only way that a society can raise the real wages of all its workers is to increase the amount of savings available per worker.

For example, American steel companies need an investment of some $20,000 per worker, for workers to get the high wages they are paid. In a market economy these high wages are shared by all. The barber, who has not changed his methods very much in the last century or two, competes in the labor market with steel workers, each of whom uses about $20,000 of equipment. Wage rates of all workers are thus set by the average savings available to help workers increase their production. These higher wages and lower prices must appear before the savers can get any of their money back, much less any interest or profit on their speculative investment.

Profits may come, but they can only come later if buyers, of their own free will, decide that the new market offerings are better bargains than all other available goods and services. This is the secret of progressively higher living standards in a free market society. The secret of higher wages is more savings per available worker. A man with a modern expensive earth-moving machine can move far more earth than the strongest man using his hands or even a shovel. As more and better tools become available and as more goods are produced, there will be a higher standard of living for everyone who participates in the market economy.

Effect of Present Union Policies

Consider now the effect of present-day union policies upon our economy. The essence of labor union policies today is (1) to restrict production and (2) to prevent the unemployed, or those employed at lower wages, from improving their economic situation by underbidding union-imposed wage rates. We cannot improve the general welfare by following union policies that restrict production by making high wages higher for some workers, with the result that low wages are kept low or nonexistent for other workers.

Whenever union workers get a raise above free market wage rates, this increase raises production costs, and as a result prices must be raised to consumers. With higher prices, fewer goods are sold. When fewer goods are sold, some of the workers are laid off and the laid-off workers must then compete for the lower-paying jobs. Their competition in these next lower-paying jobs drives some previously employed workers out of jobs. This forces their wage opportunities still lower. Such policies restrict production and keep men from working where they can produce the goods most wanted by society.

Much of this is, of course, due to the popular fallacy that only an equal exchange is a fair exchange and that if one person, the employer, for example, gains, he must have done so at the expense of the worker. This is responsible for so much of the antagonism against the capitalist, against the investor, against the saver — the belief that his gain is unearned and that the capitalist or saver is getting something at the expense of the worker. This is Karl Marx's exploitation theory. It is the theory of class warfare as opposed to the market theory of voluntary social cooperation.

Marx put great stress on this. He believed that under the natural law of wages, employers worked the workers too long. Workers produced enough to support and reproduce themselves in, let us say, ten hours. Employers worked them eleven or twelve hours. According to this idea, what workers produced in the extra hour or two was taken and kept by the capitalists. So one of the chief policies of labor unions has been to demand shorter hours for the same pay. If you shorten hours for the same pay, you have less production. Less production does not provide a higher standard of living. If widely practiced, it must mean higher prices and a lower standard of living. Of course, when this happens as a result of free market processes, it means that market participants prefer to take some of their potential increased production in the form of more leisure.

Another fallacy in this area is the argument that money wages must be raised in order to provide workers with the purchasing power to buy their production. Actually, higher living standards require more production, not more money. Workers can only buy what is produced. If production is reduced because fewer workers are hired, increasing money wages does not provide any more goods. This is an old fallacy. There is no way to increase the purchasing power of one worker by increasing his wages without at the same time decreasing the purchasing power of other workers.

The employer has no power to set wages. He cannot in the long run pay more than the consumer will repay him. Nor can he long pay less than the market value of labor's contribution. This Marxian idea simply does not stand up. Yet, today many people honestly and sincerely subscribe to this idea that employers have too much power. Their failure to understand free market economics permits them to believe that in a modern industrial society employers have great power while the poor workers are helpless. Actually, in a free market society it is ultimately the consumers who set prices and thus the wages that employers can and must pay.

How Labor Unions Affect Wages

Questioning the virtues of organized labor today is like questioning or attacking religion, monogamy, motherhood, or the home. In public opinion, the test of whether one is for or against labor or the workers or the poor in general is your attitude toward labor unions. One simply cannot argue that certain union policies hurt labor and expect to be taken seriously. The fact is, of course, that union policies *have* hurt workers in general and particularly those at the lower end of the income scale.

The essence of present-day union wage policies is to reduce production and to keep the unemployed from finding work and the low-paid from competing for higher-paying jobs. Such policies are not going to raise the nation's standard of living. We can never improve the general welfare by policies which reduce production. Unions make high wages higher for some, but they make costs higher for other people and thus reduce the goods and services that consumers, including workers, can buy in the market place.

The unemployed, those at the bottom of the economic ladder, have no voice in union affairs or in setting wage rates. They are completely shut out. Union officers care very little about nonmembers or beginners trying to get started. There are cases in New York where a man cannot get into a union unless his father was in it before him. Since, under the law, only union members can work in certain trades, this has hurt Negroes trying to enter trades white unions have monopolized. If one's father had to be in the union, how can a Negro ever get into that union? This has applied to other low-income minorities in times past. The unions do not help the relatively poor. They help the aristocrats of labor at the expense of low-income workers. They get privileges for their members at the expense of other workers or would-be workers and they raise prices for all consumers.

Combinations of workers can only raise wages if they can raise the value or the *quantity* of the product that they produce. Now, of course, if the quantity produced is smaller, other things remaining the same, the value per unit is greater. However, the available quantity will satisfy fewer consumers and thus provide less human satisfaction. So, if the unions do not increase production, the only way they can raise the relative value of a unit of labor is to reduce the units of labor employed and the quantity of goods produced in that industry. Without the power to keep out other workers, unions can do little to raise the market value of what their members produce. This does not help either the workers excluded or consumers in general.

We live in an age of mass production for mass consumption. If we do not have mass production, we cannot have mass consumption. So by reducing the amount of production, unions are not helping workers in general. By setting wages at higher than free market wage rates, unions reduce the amount that can be sold. They throw people out of the jobs where they could be most productive. What the unions gain for their own members results in a loss to those who are excluded from cooperating in the task, and it results in a loss to all consumers as they will have to pay higher prices per unit for a smaller quantity of goods and services. Every consumer who does not share the union's gains will have to go without something he could have bought *if the union gain had not* raised prices.

The control of wage rates is also the control of entry into a trade or industry. Such control also determines rates at which a company or industry expands or contracts. In a free society, if the wages in an industry were lower than those forced by unions, that industry would expand. When unions raise the wages of an industry, that industry either has to contract, or, if it stays the same size, it is prevented from expanding as it would if it could pay free market wages.

Expanding means paying higher wages to attract the more workers needed. It also means producing more goods that consumers want most and lowering prices so the same wages will buy more. Of course, there is also a tendency toward the elimination of profits. Unions can protect their members from the competition of other workers merely by raising union wage rates, because then the employer cannot afford to employ any more. This is one of the inevitable results of the union seniority principle. Those with high seniority are not worried about those who lose jobs because of higher union wages.

Effect of Union Policies on Savings

One of the most important factors in the labor situation is the effect of union policies on employers, savers, and investors. Many think that wages can be raised at the expense of the employer or the investing owners, and thus higher wages need not hurt the consumer. They think you can just reduce profits a little bit more and that will take care of the higher wage costs. As we have tried to make clear, the way to raise the wages of workers is to increase the savings invested in tools that workers can use to increase their production.

The accompanying table may help to give us a better understanding of some of the problems faced by workers and by those who try to make a living by employing people. Assume a steamship which cost $2 million to build and which is expected to last 20 years. The yearly depreciation and interest charge would then be $150,000. The owners assume an expected market revenue of $14,100 per week. It is expected to operate 50 weeks of the year. The people who are investing this $2 million considered it carefully in advance. If their forecast is correct, they expect their weekly costs will be:

Depreciation and interest	$3,000
Labor wages	8,000
Other operating costs	2,100

and they hope for profits of $1,000 over and above the interest which they could get by lending the money out. The total of the items mentioned comes to $14,100.

Of course, if they foresee future developments incorrectly, they will suffer a loss. But if they have foreseen future operations correctly, if they have calculated their labor and other costs correctly, and if they have estimated correctly what the public will pay for the service, then and then only will they earn the estimated profits. Then only will they earn the estimated profit and be able to replace the ship and continue to employ the workers after 20 years.

In order to make this problem easy to understand, we shall assume that this ship is on a lake and cannot be moved to be used any place else. So once this investment is made, those who have

Steamship Costs $2 Million and Lasts 20 Years
Yearly Depreciation and Interest Charge—$150,000
Market Revenue $14,100 per Week (50 weeks)

Weekly Cost	Free Market Wage Rates	Union Forces Wages Up 10%	25%	50%
Labor Wages	$8,000	$ 8,800	$10,000	$12,000
Other Operating Costs	2,100	2,100	2,100	2,100
Depreciation and Interest	3,000	3,000	2,000*	none*
Profit	1,000	200	none	none
Totals	$14,100	$14,100	$14,100	$14,100

*Amount available toward $3,000 expense.

turned their savings into a steamship cannot withdraw them. If a labor union has the power, either through public opinion or through the laws of the land, to raise wages above those prevailing in the market at the time, the investors will then be at the mercy of the unions.

Now, we shall assume in the second column of figures that the union is able to threaten a strike or otherwise use its power to raise wages 10 per cent. This increases the cost of labor to $8,800 and reduces the profit, beyond the charge for interest, to $200. Under such a situation, the owners will continue operating. They will still get a small profit, smaller than they had calculated, yet more than they would have gotten if they had lent their money out at market rates of interest. They are still – you might say – ahead of the game.

The union members, having found it easy to use their power to get this 10 per cent increase, are still not satisfied. They try it again. Let us assume that this time they increase wages to 25 per cent above free market wages. You see the results in the next column – a situation in which the workers are then getting a weekly total of $10,000 in wages. There are no longer any profits after interest. In fact, the employers are not covering their depreciation and interest. They are only getting two-thirds of this expense, or $2,000. Under such circumstances, they will still operate the steamship. If they stopped operating, they would get nothing for depreciation and interest. $2,000 is better than nothing. Everyone prefers a little something to nothing. We even prefer a small loss to a larger loss. At this rate, when the ship is worn out, the owners will not be able to replace it. They will not have depreciated enough. So, of course, when the ship is worn out, this business will be ended and the men will lose their jobs.

But assume the union workers do not see this. Suppose they go on and ask for a further increase. This time we assume they seek a total increase of 50 per cent. Then you find the situation in the last column where you have arrived at the margin. The owners receive nothing for their capital, no allowance at all for depreciation or interest on their capital. The operating income would just cover the wages of the workers and other operating costs. Then, it no longer pays the investors to operate their steamship. They have reached the point where they would be operating the ship for nothing. This they do not care to do. So the operation comes to an end and the men lose their jobs. They have killed a good thing.

Savers Can Be Scared Away

All this is not very far from reality. For many years, from 1837 to 1947, we had in the United States the old Fall River Line. It was a steamship line that provided overnight boat service between the beautiful harbor of New York and Fall River, Massachusetts, a short train ride from Boston. It was a trip that many people enjoyed and a cheap way to ship freight. The unions kept raising the wages of their members until the steamship line was forced out of business.

There are lessons to be learned from this illustration. Businessmen can get caught. Investors can get caught. Savers can get caught. Once they put their money into particular forms of capital they are caught. When unions can raise wages to the point that business income covers only part of the depreciation and interest expenses, the investors will still operate their business, because any income is better than writing off the investment as a complete loss. But what is the effect of this on potential investors? Would you, if you had any savings and saw this happening, try to go into competition or start a similar service elsewhere?

This is the problem that workers face. Yes, unions can temporarily raise some workers' incomes. But they also reduce the competition for workers and in the long run they reduce the number of high-paying jobs available. In real life, tools, machines, and other capital goods wear out or become obsolete one by one. They do not all go to pieces at one time. A typewriter wears out and it is replaced. Some small machinery wears out from time to time, but whole factories seldom wear out all at once. Unions can push wages up so long as it still pays to replace the worn-out parts and continue operations. This permits businesses already established to stay in operation, but it greatly discourages the starting of new businesses.

These union policies thus tend to stifle the very thing that encourages competition for workers and raises wages. If we are to have higher real wages, higher real income, that is, more goods and services, we must have more savings and more businesses competing for the workers. This union policy, of forcing wage rates above those that would prevail in a free competitive market, reduces the savings and the number of employers who compete for workers. Under such policies, people with savings will tend to put them under the mattress or send them out of the country.

There are many people in many parts of the world who are sending their savings outside of their country, just because of such conditions. They no longer feel that it is safe to invest savings in their own country. Other people stop saving. Why save, if your savings are going to be confiscated? Why not spend, live high, and have a good time while you are here? Still others will put their savings in government bonds in the belief that they will be safer there than invested in private enterprises. But the money will then be spent to buy votes and the interest on the government's debt will become an added burden on the taxpayers and on the workers too. So we see that if union wages are forced up above free market wage rates, they end by killing the goose that lays the golden eggs of higher wages for all, that is, the increased invested savings that provide higher and higher standards of living for all.

Only Savings Can Reduce Economic Hardships

The reason why we have so much starvation in so many countries, in India for instance, is because private property is not protected. Investments are not protected. After India became independent of England, Nehru said that India needed and wanted foreign capital. It is true, he admitted, that India was going to be socialist but he added, if you will put your capital in India, we will promise not to confiscate it "for at least ten years." How much money would you or any sane person invest in India under such conditions?

If workers want to raise their

wages, they must adopt policies which will encourage savings. We have had this problem in the Western world for a good many years now, for most of this century. However, as union wages have gone up in the more productive industries, which unions can most easily organize, and in what we call bottleneck industries, like transportation, the unions can shut down other industries. They raise the wages of some, but raising wages raises the prices, and with higher prices fewer articles are sold, which means fewer men are employed in the organized industries. The workers kept from jobs in these industries must then compete in some other lower-paying industry. This drives those wages down unless those workers too are organized into politically privileged unions. Then more workers are thrown into competition with still lower-paid workers, until some of them are, by these very "pro labor" policies, forced to work for wages on which they cannot keep body and soul together. Then we feel sorry for them.

The popular remedy today for such very low wages is a minimum wage law. The minimum wage law says that you cannot employ a man unless you pay him a specified minimum wage. In the United States, this is now $1.60 an hour. We still do not have a dictatorship. Until we do, employers will only employ people if they can hope to get the $1.60 back from consumers. If the consumer says a man's contribution is only worth $1.50, the employer is not going to pay him $1.60.

The employer is only an agent of the consumer. So the man becomes legally unemployable. It is now illegal for anyone to hire him. He cannot legally earn what he could in a free market, which is to say, the highest amount any consumer will pay for his contribution. So unemployment insurance was invented to take care of these people. When unemployment insurance payments expire, the popular remedy is relief or welfare payments, which become a burden on taxpayers who are, of course, in the long run, the workers. The only possible outcome of such policies is higher prices, higher taxes, less production, and more poverty.

Good Names for Laws Not Enough

People with the best of intentions and the least economic understanding constantly try to help the people on the bottom of the economic ladder by governmental intervention. We have had the National Recovery Act, which was supposed to help both business and labor by letting them organize with government help to set high prices and high wages. We had the Agriculture Adjustment Act. We had the Securities and Exchange Act. We had many such acts with nice sounding names and preambles expressing the best intentions.

The real question always is: Are such laws a sound means for obtaining the desired or specified ends?

The National Recovery Act did not produce national recovery. The Agriculture Adjustment Act did not adjust agriculture to consumers' wishes. We have had surplus after surplus. We have given billions of taxpayers' dollars to the farmers and after thirty-five years still do. The so-called farm problem is still with us. Only one such law has lived up to its name. The Unemployment Insurance Act has guaranteed that we will have unemployment.

These interventions did not increase production. In a free market society everybody can get a job at the highest wage the consumers will pay for his contribution. He cannot long get any higher wage; and nothing that government can do will change this situation or improve it. But many workers and voters believe unions can raise the wages of all workers.

Governments, of course, have to do what is popular; they cannot do what is unpopular. Today it is popular to think that no worker's wages should ever be allowed to fluctuate downwards. Wage rates, it is thought, should only move upward. So our laws and labor unions attempt to prevent any reductions in money wages.

The market system permits consumers to change their wishes and wants. When these shift, employers have to change the things they produce to satisfy the customers. The way this happens in a free market is that the prices of things no longer wanted in such large quantities go down, while the prices of things for which demand has increased go up. Businessmen switch from producing losing lines of goods to producing goods on which they hope to make a profit. They stop producing goods that can only be sold at a loss. When the demand changes, they make fewer candles, for instance, and switch to producing electric bulbs and lamps. And so it is that workers must switch to different industries.

Nowadays, we no longer permit any wages to fall. So if employers can no longer pay the union-demanded wages, they must cease operations altogether and fire everybody, including those who might be satisfied with slightly lower wages until they can find better-paying jobs.

Employers and Employees Not Enemies

In real life, workers and investors in the same company are not competitors. Production and marketing are not class warfare. Savers, employers, and employees of the same company are team workers. A demand for a Ford automobile is a demand for a Ford factory and for Ford workers. All those needed to produce the factory and the autos are a team. Anything which helps an automobile company helps all those who are on the team, either as investors or workers. The ultimate demand of consumers is for a team combination and it is this free combination that is going to help all of us have more of the things we want most.

The demand for workers at higher wages should come from those putting increased investments to work. New investments always seek new workers. Then all other employers have to pay the new higher wages, because no employer can keep workers if a competitor is offering higher wages. Present union policies cannot raise the wages of all workers. They lead only to higher prices and lower production.

If we are going to stop the ever upward wage-price spiral before there is a complete collapse in the value of the monetary unit, we must create a climate that will lead to the repeal of all laws which permit unions to exclude qualified workers from competing for jobs in union-organized industries. We must stop subsidizing unemployment and permit wages to be set by free market competition in the service of consumers.

The Keynesian Solution

This is not the policy in most countries of the world. Under present policies, workers are getting higher money wages which are lower real wages because the value of the monetary unit is constantly being diluted. We are going into progressive inflation. Savers are being liquidated. Their property is being confiscated. New savers are scared away.

Politicians are constantly afraid, and rightly so, of doing things which are unpopular. They endorse popular spending measures, but they shun the resulting costs; and to stay popular they have resorted to inflation. This is the so-called Keynesian policy. It is set forth in John Maynard Keynes' book, *The General Theory of Employment, Interest and Money*. The key sentence is: "A movement by employers to revise money wage bargains downwards will be more strongly resisted than a gradual and automatic lowering of real wages as a result of rising prices."

This was the policy endorsed by Keynes. It is the policy of most governments in the Western world today. Keynes knew, as every economist does, that the only way that you can employ more people is to lower the wage rate. But ever since World War I this had become politically difficult in Great Britain. Powerful British labor unions, with the help of the Fabian Socialists, had built up public pressures which opposed any lowering of any money wages. British politicians of all parties were afraid to resist this popular union policy. So in 1931, when the number of unemployed became unbearable, the politicians in office preferred to lower wages by devaluing the British pound. The workers kept their puffed-up pound wages but their pounds bought less.

In 1936, Keynes gave this political policy academic sanction in the book and sentence just quoted. Since then, most Western nations have adopted this "Full Employment" policy. In essence, when unemployment is considered too high, wages are lowered by lowering the value of the monetary unit. This is done by increasing the quantity of the monetary units. We have gotten into a situation of ever-rising wages and prices with more and more workers paid less than they would earn in a free market.

Neither union leaders nor union workers are stupid people. Keynes and the British politicians were able to fool the employees in England when they first tried this scheme in 1931. They changed all the index numbers, making it difficult to document the price rises reflecting the lower purchasing power of the pound. But now every union has a statistician, who can see from the official cost of living indices that prices are going up. And when they go up, the unions demand still higher wages. This system of Keynes' has just about reached the end of the road. You can no longer fool the workers by lowering the value of the monetary unit. They are now wise to what is happening and they are not going to take it much longer.

The only final answer to this problem is more economic education showing that the only way to keep raising wages permanently is to increase production and the way to do this is to encourage savings. For it is only increased savings that can provide workers with more and better education and more and better tools with which they can produce and buy more and better products that they want most.

Photo by Chris Honeyman

Ludwig von Mises

DEAN OF RATIONAL ECONOMICS

HANS F. SENNHOLZ

WHEN, in future centuries, historians search for the reasons for the phenomenal decline of Western civilization, few contemporary sources will be of any use. True, they offer colorful descriptions of the symptoms of this decline, but their explanations are usually infested with the very bacillus that is destroying our magnificent order. Future historians will be bewildered about our blindness and madness, our moral lethargy and decay.

"But were there no 20th Century philosophers" they will ask, "who recognized the ominous trend toward economic destruction, social disintegration, and political tyranny? Was there no prophet of the impending doom?"

We hope for their sake that they will discover the works of Ludwig von Mises who, since the beginning of this century, has been warning his contemporaries. Again and again he forewarned them about the growing popularity of ideologies of conflict and war, the rise of collectivism, and the sway of tyranny in the Western world. In fact, his writings, which will be so invaluable to future historians, are last-minute warnings to us, the living generation.

This is why the Foundation for Economic Education in Irvington-on-Hudson, New York, in conjunction with Arlington House in New Rochelle, N.Y., and Jonathan Cape Publishers in London, have again prepared new editions of some important Mises works.

Socialism, An Economic and Sociological Analysis (Jonathan Cape, 30 Bedford Square, London)

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