MARGINAL UTILITY AND VALUE

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In the *Quarterly Journal of Economics* for October, 1890, under the caption "Boehm-Bawerk on Value and Wages," I gave some reasons for doubting the claim of marginal utility to be regarded as the regulator of exchange value. Professor von Wieser of the University of Prague has done me the honor of replying to my objections. In an article published in the *Annals of the American Academy of Political and Social Science* for March, 1892, he explains and defends the position of the Austrian economists, taking occasion at the same time to expose the defects which, in his opinion, are inherent in the classical theory of value. The Austrian theory has attracted so much attention, and has at the same time received so little critical examination in English, that I take the liberty of asking space for a brief discussion of it.

The points at issue between the new theory of value and the old are reducible, I think, to two fundamental questions: 1. What is the true nature of cost of production? 2. What is the true connection between cost of production and value? At least, it seems clear that the fate of the Austrian theory of value depends on the ability of its advocates to answer these questions in a satisfactory manner. I propose in this paper to inquire how far their treatment of these matters up to the present date can be accepted as satisfactory. In doing so, I shall confine myself, in the main, to Dr. von Wieser's article mentioned above, as the latest authoritative statement, making use, however, of other publications by members of the school, whenever additional light can be obtained thereby.

I.

The most striking feature of the Austrian treatment of cost is that it makes value the measure of cost. The cost of each commodity consists in the value of the means of production necessarily used up in producing it. Even human labor is regarded as an element of cost only in so far as it has value. That is to say, the primary element of cost is not the labor itself, but its value. Since this is a point of great importance, it is only fair that we should have it in the words of the authors themselves. Dr. von Wieser explains the nature of cost as follows:—

Every capitalist must in his own interest adapt his business to the general conditions of the market, if he wants it to maintain itself profitably. So far as he resorts to means of production that have other applications as well, he finds that they have a given value. He must pay for them, and the value of the goods he produces must replace this expenditure. In this sense, he has to adapt the value of the commodities to the value of the means of production. Thus originates the conception of cost. Cost consists in means of production having manifold applications, like iron, coal, and common labor, which, even when they are employed in the production of a single commodity, are still estimated according to the value they have in all their applications. The hundreds and thousands of different kinds of materials and tools prepared for production are counted, weighed, and measured according to the utility which they are to create, and in view of their importance most jealously guarded by their possessors. In the same way, the different kinds of labor are assorted according to the utility expected from them, and arranged according to a classification which differs essentially from that which would result if the effort involved should be taken into consideration. The unlimited possession of useful productive materials and forces forms the basis of the economic confidence of modern society. Since each productive process diminishes this possession, it *costs*,— and it costs exactly as much as the value which the material and labor required would have produced if rationally applied. (p. 41.)

Again:—

Our principle is that value is derived from utility; and, quite in harmony with this principle, we assert that cost is, after all, according to the general law of value, that of marginal utility, measured by utility alone. (p. 44.)

Obviously, there cannot be two independent laws of value. Two independent regulators of value could not always coincide in fixing one and the same value. If marginal utility fixes exchange value, then clearly cost of production does not also fix it. In order to avoid the obvious conflict, the Austrians have undertaken to show that marginal utility fixes cost as well as value. There was, indeed, no other way out of the difficulty. If it can be shown that they fail in this undertaking because they ignore true cost altogether, no further proof is really needed to show that the control over value claimed for marginal utility has not been sustained.

The treatment of cost by the Austrian economists has, I think, two serious defects. In the first place, they set out with the value of such things as iron, coal, wood, and land as factors in the cost of production of the commodities in the making of which these articles come into play. They begin the computation of cost by assuming the value of materials as an ultimate element in cost, as if no inquiry into the history or antecedent conditions of these materials could be in order. Dr. von Wieser writes precisely as if the man in the moon supplied men with iron, coal, and other materials, in quantities fixed by his own sovereign fiat, at values set by the marginal utility of his wares to us. In other words, the Austrian computation of cost of production begins, not at the beginning of the process of production, but at a selected point well along in the process. The cost of production of iron palings, for example, is contemplated as beginning at the point where pig iron is appropriated to the making of palings. Apparently because iron may be brought to the stage of pig without being committed to this particular use, they do not regard the mining and smelting of iron ore as any part of the process of producing iron palings. This procedure may have advantages for their theory, as well as a certain appearance of reasonableness. Obviously, if cost is to consist in the "value of the means of production," the reckoning of cost cannot begin until value has appeared. So iron in its original ore-bed is not a means for the production of palings, since in that form it has no value. When it has been dug out and smelted into pigs, it has a value, and becomes a "material" or a "means" for the production of palings or any other of the ten thousand things made of iron.

But what, on this method, shall be said of the labor of mining and smelting? Is that no part of the labor of producing iron wares? In the economic sense, which is but another word for the true sense, I see no possible ground for denying this character to such labor. The fact that some materials are adapted to the production of many different sorts of commodities does not in the slightest degree affect the nature of the process of production. That remains for each commodity of the group precisely what it would have been if the other members of the group did not exist. If iron palings were the only commodity made of iron, I suppose the Austrian economists would admit that the labor of mining and smelting iron ore is a part of the labor of producing iron palings. It is, then, incumbent on them to give a clear and conclusive reason for holding that the use of iron for making other products makes it necessary for us to treat the cost in a different way. . The difficulty of foretelling, before differentiation begins, what particular use any given portion of iron ore may be devoted to, does not alter the fact that every portion of it does go to some particular use. There would be no greater difficulty in separating costs at this stage than at any and every other stage of producing things under our highly complicated system of combination of labor. Whether we regard cost as consisting in necessary exertion or in the value of the means of production, there are difficulties in the way of tracing accurately the cost of any given commodity. The Austrian view may mask these difficulties somewhat, but I think it does not really evade or diminish them in the least. At all events, the fact is clear that the labor of digging out the ores of iron and the other metals, of getting wood from the forest, of raising cotton, linen, wool, and all similar "means of production," is productive labor. If it be a part of the necessary labor of producing the goods in the making of which iron, tin, cotton, wool, etc., come into play, what good reason can there be for refusing to recognize it in our definition of cost, on a footing of equality with the later labor? If, on the other hand, we hold that it has no place in the cost of these goods, what shall we do with it? How shall we classify it, and what shall we assign as its economic motive? For my own part, I can see no valid reason for treating it differently, in relation to cost, from the labor of the later stages in the production of each commodity.

The Austrian economists seem to have held that no reason is necessary. The only suggestion I have met with in their writings, that seems to bear on the point, is to the effect that we cannot in any case get back to the very beginning of the production of any article. Even in the making of our tools for use in procuring the materials of any given commodity, we have the use of old tools. This suggestion opens up a large question, as to the proper way of treating capital in relation to cost of production. Dr. von Wieser holds that capital must be regarded as a separate factor in cost, distinct from labor and waiting, or labor and abstinence. "Everywhere the new capital is the descendant of previously existing capital. By no form of computation can the factor 'capital' be eliminated from the cost of capital." He is so impressed with the weight of this consideration that he is unable to avoid a suspicion that English and American economists, finding themselves unable to explain the relation of capital to cost, have entered into a conspiracy to say nothing about it. I must take the liberty of doubting whether he has quite understood the position of those who reduce cost of production to labor and waiting (or abstinence). He argues as if adherents of the classical theory reduced cost to labor alone. We are certainly as free from that error as the Austrian economists. The only real question between us is how to treat the other element in cost. The Austrians propose to call it the value of the capital consumed in producing each commodity. The classical economists urge, in objection, that capital is itself a product of labor; that, therefore, if we name the necessary labor of production as an element of cost, we should be guilty of double counting if we name the necessary consumption of capital as a further element. To this objection Dr. von Wieser replies that "nowhere in our modern economy is capital produced by labor alone." Since, in the making of our new capital, we have the use of old capital, he thinks the consumption of capital must be regarded as an element in cost distinct from, and in addition to, the necessary labor and waiting. But I think he overrates the importance of this consideration in its bearing on the analysis of cost.

In the first place, the fact that we have, in every productive undertaking, the use of previously existing capital, seems to be a poor reason for Dr. von Wieser's own mode of treating cost. The fact that we have the use of old tools in the making of new ones does not obliterate the fact that both the new and the old are products of human labor. Granted that we have the use of old mines, forges, and machine-shops in making the necessary outfit for opening and operating new mines, I fail to see in that fact the least reason for ignoring altogether, in the cost of producing iron wares, the labor of digging out the ores and smelting them into pig iron. Why begin with the value of pig iron, as if that were an ultimate fact, when we