THE MEANS TO FULL EMPLOYMENT

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EUROPE, RUSSIA, AND THE FUTURE

GREAT BRITAIN IN THE POST-WAR WORLD

THE MEANS TO FULL EMPLOYMENT

by

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CONTENTS

INTRODUCTION

This is a book about the things that we need to do in order to abolish unemployment, or at all events to reduce it to such small dimensions that it need no longer be regarded as a serious social problem. The things that need doing in order to achieve this result are, I believe, pretty plain; and there can no longer be much dispute about them, though there can of course be differences of opinion about how far they ought to be pressed. If the problem of getting rid of unemployment could be regarded as simply a technical problem—that is, one of devising the right means for the achievement of an accepted end—there would be very little difficulty about it, even if some of the appropriate remedies would take some time to apply. Cyclical unemployment, treated simply as a technical problem, could be got rid of quite easily and quickly by action on an international scale, and could be, if not got rid of, very greatly reduced by action confined to a single country. 'Structural' unemployment—that is, unemployment due to faults in the capital structure of industry and in the nature and distribution of skills among the human agents of production—would take longer to deal with adequately; but here too the character of the required remedies is, in the main, fairly clear. We do, nowadays, know pretty definitely how to deal with unemployment—if that is what we want to do.

But is it? The difficulty is that unemployment is not a purely technical problem: nor is its abolition an aim which everyone is prepared to pursue without any reserve. It is one among a number of things which are regarded as desirable in themselves, but not in all quarters as desirable absolutely, without regard for the price in terms of other objects which may have to be paid. If we could abolish unemployment and, in doing so, leave everything else unchanged, we should doubtless be ready, without further controversy, to put into effect the measures recommended in this book. But, of course, the carrying out of these measures would not leave other things unchanged. It would alter a great many things and, in doing so, would offend a good many people to whom these other things either matter more than the abolition of unemployment, or appear as 'rights', which they are not prepared to allow to be infringed.

To begin with, it is plain that the abolition of unemployment means a large increase in the extent of government intervention in economic affairs. But there are a good many people who dislike government intervention in their businesses much more than they want to get rid of unemployment. There are, most obviously, the monopolists, who do not want to be made to give up practices which keep down the demand for labour by limiting production; but in addition to the monopolists there is also the very large number of persons who dislike being 'badgered about' by officials, and to whom increased government intervention holds out the prospect of being 'badgered' more than ever. Then there are Trade Unions of skilled workers, who dislike the prospect of the Government taking a hand in training workers to compete in their several crafts, and regard proposals to make labour more 'mobile' as so many attempts to break down their established standards of wages and conditions. There are both employers and Trade Union leaders who do not want to see the Government overriding the methods of collective bargaining to which they are accustomed; and there are still some economists who believe in the divine inspiration of *laissez-faire* doctrines, and would sooner see the whole world perish of starvation than admit that these doctrines may be wrong. There are persons—I am myself among the number—who cannot abide highly placed Civil Servants, and will be strongly tempted to oppose anything that is likely to increase their power. Finally, there are Socialists who have convinced themselves that Socialism is a cure-all and nothing short of Socialism a cure-anything; and even, at the other extreme, persons—I have met some of them—who are convinced both that the unemployed could all get jobs if they wanted to and that none of them are worth employing, so that there is nothing that needs to be done.

I have not included in the foregoing enumeration those who make use of the argument—quite frequent in these days—that we ought not to want to get rid of unemployment, because unemployment is the price of freedom. "Look at Germany!" such persons exclaim. "Look at Russia!" "Look, even, at wartime Britain." "Nazi Germany abolished unemployment by enslaving the workers." "Soviet Russia abolished unemployment by enslaving the workers." "Even in Great Britain, we have got rid of unemployment only by conferring on the Minister of Labour the most arbitrary powers to make anybody go and work anywhere under orders." "Freedom to move from job to job as you please involves unemployment: unemployment is the price we have to pay for having labour free instead of enslaved."

Is that really true? Must we live either under the constant threat of unemployment, or as slaves? Is it by enslaving the workers that the Nazis, or the Russians, had got rid of their unemployment problem in time of peace, and that we have got rid of ours in time of war? I do not think so. That the Nazis have enslaved the workers I agree; but I do not think that was how they got rid of unemployment. They got rid of it by making the Government, and not the profit-seeking employer, the arbiter of production and employment, by following a policy of public investment which kept the industries producing capital goods and armaments busy—by producing so many 'guns' that there was only just enough labour left over to produce the indispensable minimum of 'butter'. If they had not held the working class in firm subjection, if Trade Unions had been left in being and there had been no political police to make a short way with agitators, they would have been compelled to produce more 'butter', and fewer 'guns', or unemployment could not have been prevented. The enslavement of the workers was essential to their policy of intensive, aggressive armament for war. But it was not essential for getting 'full employment'. Suppose the Nazis had been angels instead of devils, and had been set on producing 'butter', instead of 'guns', why should they not have done so? As soon as the Government, with whatever end in view, arms itself with the power to determine the volume of production, and takes this power away from the profit-seekers, the power to abolish unemployment comes to rest in the Government's hands.

The leaders of the Soviet Union, for their part, wanted to make 'butter', though they were forced, in self-defence, also to make a great many 'guns'—and we can be heartily glad that they did. Did they, in getting rid of unemployment, enslave the Russian, as the Nazis did the German, working class? Surely not. They did, no doubt, make use of forced labour as a definitely penal measure, against the *kulak* class which they were determined to liquidate. But Russian policy in the timber-camps had nothing to do with the abolition of unemployment. The men who were sent to the timber-camps or to dig the new canals were not unemployed; and these 'public works' were not started at all for the purpose of 'making work'. They were started because they were urgently needed; and the problem facing the Russians, despite their numbers, was one of shortage rather than superabundance of labour. There was no unemployment, beyond a little 'frictional' unemployment in a few places, in the Soviet Union, because the Russians were straining every nerve to produce as much as they possibly could. They were struggling with all their might to do simultaneously three things which made competitive claims on their productive resources—to industrialise, to arm for national defence, and to raise the standards of living among the Soviet peoples. Where the Nazis were crying out for 'guns' before 'butter', the Soviet leaders wanted 'guns' and

A 2

'butter' and the means of making both, all at once. There was no room for unemployment under such conditions.

It is, however, obviously true that in any country which makes the highest possible production its aim, whether its objective be 'guns', or 'butter', or both, the rulers will be under a strong impulsion to try to make the people work a good deal harder than many of the people want to work. There are three ways in which this can be done. The people can be induced to work harder by the offer of large material rewards for increased output; or they can be induced to work harder under the spell of an idea or an emotion of service; or they can be driven to work harder against their will by fear. The Russians could, but the Nazis could not, make large use of the first of these methods; for the rewards must take the form of 'butter', and more 'butter', beyond a very limited amount, meant fewer 'guns'. The Nazis had to keep down the standard of living of the German people, as an indispensable part of their policy of preparation for war. They did try, wherever they could, to use the second method, by indoctrinating the German people with Nazi ideas of glory and race-superiority. But, especially with the older workers, they had to rely mainly upon fear.

Now fear, as an incentive to high output, operates in ordinary circumstances mainly in the form of a fear of losing one's job, a fear of being unemployed. Fear in this form, however, could not be invoked effectively, because the Nazis wanted the product of everyone's labour and could not afford to keep a labour reserve large enough to maintain the fear of unemployment in the workers' minds. They had, therefore, to evoke fear in other forms—to drive the workers to unremitting labour by the fear of condign punishment. They had to enslave labour, as the only means of getting it to work as hard as they demanded of it when the fear of unemployment had been removed.

The Russian leaders also wanted to drive the Soviet peoples at a hotter pace than they were likely to find at all comfortable—the more so because most of them were new to the discipline of the modern machine. But in this drive Stakhanovite inducements and idealistic appeals played the main part. Piecework inducements could be used on a large scale (much to the scandal of many sentimental Socialists) because the fundamental aim of the Soviet Union was 'butter' and not 'guns', so that higher real wages were welcomed as signs of progress, instead of being regarded as so much waste 'butter' that might have gone to making 'guns'—pretty much as the capitalists of the Industrial Revolution regarded all wages above a bare minimum as so much loss of capital for accumulation. Moreover, the Soviet leaders could appeal to the idealism and sense of comradeship of their people with much less difficulty than the Nazis, and could trust the workers with power instead of needing to suppress all forms of combined working-class action. Consequently, Trade Unions and workshop democracy could flourish in the Soviet Union, whereas the Nazis had to put such manifestations of solidarity down with a strong hand. Even so, the hot pace which had to be set in pursuance of the attempt to achieve all three things—industrialisation, armament, and a rising standard of life—simultaneously did mean a sharp discipline in the factories, but a discipline which was in the main self-imposed by the workers, so that it was felt, not as slavery, but as collective service to the new social order which it was devoted to consolidating and securing against attack.

In Great Britain, the war, at any rate after the collapse of France, brought into play a situation and a spirit akin to that which had existed for years before in the Soviet Union. With every month of total war the pressure on man-power became more severe; but at the same time the sense of national danger and the will to resist Nazi aggression created the spirit which made men and women willing to work at a hotter pace and to put up with hardships and inconveniences which would have been strongly resented in time of peace, or even during the earlier stages of the war. The critical 'Battle of Britain' was fought and won for the most part not by the exercise of compulsory powers, but by a spontaneous national effort. If Inkerman was a 'soldiers' ', this was a workers' battle. This experience made the nation ready to accept compulsion to go on doing what it had begun by doing of its own free will. Mr. Bevin was able to impose his orders calling up women for military and industrial service and compelling men and women to go and work where they were needed most, not merely without resistance, but with almost general consent. The emergency was felt to be so great that nearly everyone acquiesced in being put under orders. It is, however, plain that there were limits to this acquiescence, even in time of war. The Trade Unions were prepared to agree to any amount of dilution, but not to give up their rights of collective bargaining; the employers were ready to put their factories at the Government's disposal, but not unless they were allowed, to a very great extent, to control the 'Controls' set up for their supervision. Moreover, these things were agreed to only for the war period, and perhaps for as long afterwards as it might be clearly necessary to retain the 'Controls' in order to avoid a repetition of the disasters of the years after 1918. It was an understood thing that whoever gave up anything claimed a right to ask for it back, as far as restitution proved practicable, as soon as the emergency was at an end.

The question is, Can men have the old conditions back, and not have unemployment back with them, probably on a larger scale even than before? And, if they cannot, which will they prefer—to go back to the old conditions, or to get rid of unemployment? Each section of the community will tend to consider these vital questions in the light of what it is asked to give up, and what it expects to gain; and these expectations will differ, not simply as between employers and workers, but in very complicated ways. On the employers' side, a higher level of employment in the community as a whole means in general the prospect of improved markets, and therewith of more regular, and perhaps also higher, profits. It means less risk of loss, and a greater inducement to invest. But this incentive applies very unequally to different groups of capitalists—most strongly to those who are most fearful of post-war depression in their own industries, and least to those who feel most confident of an expanding market or of their ability to make good profits, even in depressed conditions, by the exercise of monopoly power. Each group of employers, from a purely selfish point of view, would soonest have some unemployment in their own industry, in order to weaken Trade Union pressure, and none in other industries, in order to enjoy a good market for their wares. On the other side, some Trade Unions, while wishing for 'full employment' as a general objective, probably look askance at proposals for securing it which threaten to break down their established rules and customs; while many groups of employers would think 'full employment' dearly bought if it involved taking away their right to regulate output and prices by means of monopolistic Trade Associations and agreements, or if it meant that their industries had to be subjected to special forms of government control, or even transferred to some form of public ownership and management.

On the whole, it is evident that the measures proposed in this book, as the minimum needed to secure and maintain 'full employment', will encounter much more opposition from capitalists —including some small capitalists—than from Labour. The Trade Unions will welcome most of them, even if some Trade Unions seek to obstruct them at certain particular points. Most industrial employers will probably favour those of them which involve financial changes designed to eliminate cyclical unemployment, but will be much less willing to accept the measures directed to getting rid of structural unemployment and the restrictive influence of monopoly. It will be the line of least resistance for a capitalist or coalition Government to take active monetary measures, backed up by a certain amount of 'public works policy' of a rather restricted type, but to do as little as possible in the way of action to remedy structural defects in the British economy, to combat monopoly practices, or to widen the range of 'public works policy' so as to bring about a better balance in economic development than is possible when public works are limited to a narrow field that is regarded as non-competitive with private, profit-making enterprise.

It is not possible to argue that a policy worked out on this narrow basis is bound to fail altogether; for it could undoubtedly achieve something. I hope, however, that I have given good reasons in this book for holding that its possible achievement would fall an immense way behind the need, and that any really effective policy will have to include not only monetary measures directed against cyclical fluctuations in employment and extensive public works of the traditional kind, but also drastic measures against monopoly and large steps towards structural readjustment of industry and better training of the human agents of production. I will not attempt to summarise the argument here: it is given at length in the ensuing chapters. I will say only that, in my view, an undue reliance on the efficiency of financial manipulation as against an attempt directly to improve economic efficiency will only land us in a very bad mess.

It is therefore of the greatest importance both to disabuse the public mind of a proneness to believe in the limitless prospects of financial wizardry, and to get the largest possible support for a policy which will couple the necessary financial changes with the industrial readjustments without which they cannot be made to work. My apprehension is that only a few of the more far-sighted capitalists will be prepared to support such a policy, and that the majority of capitalists, large and small, will bend all their efforts to persuading as many poor people as possible that 'full employment' means bureaucracy and slavery, and that they had better put up with unemployment, *plus* doles, than press for the extended public control without which 'full employment' cannot be secured or maintained.

One potent weapon in this campaign is likely to be the assertion that 'full employment' involves industrial compulsion; and it is essential that this argument shall be faced. It would be true, if 'full employment' meant working continuously after the war at the pace set by war necessity, or maintaining the occupied population at, or near, the level to which, including the armed and civil defence services, it has had to be raised under war conditions. Men and women will not continue to work at this pace, or under the present hardships and inconveniences, or in the present numbers, except under compulsion or under the sense of an emergency which they recognise and to which they think they can see an end. The pace that has been set in the Soviet Union over the past decades cannot possibly be sustained: there is bound to be some falling back when the men and women of the Soviet Union can at last take its stability for granted, and no longer feel that its very existence may depend on what they do. Conditions in Great Britain after the war may be such as to arouse anew the sense of critical emergency in the British people. Possibly they will; but I am not counting on it. It is safer to expect both a mood and a situation in which the intensity of effort will be in some degree relaxed, and the number of persons working outside their homes will undergo a reduction. 'Full employment' does not mean that we shall all have to go on working at the pace we have worked at since Dunkirk. It does not mean that people must necessarily go on working more than they think it worth while to work in requital for the rewards which are offered them in return for their labour.

This means that it does not imply any more compulsion to work than is implied by the sheer necessity of earning a living. As long as we do not waste labour which is ready to work on these terms, there is no reason why we should have to apply any compulsion upon those who are not. We have, however, unavoidably to take into account the effect which any measures which we adopt either to provide for fuller employment or to improve the position of such persons as remain unemployed despite these measures may have on the efficacy of the incentives we have relied on hitherto. Thus, it would be clearly impracticable, as matters now stand, to adopt a system of social security which would assure men unconditionally of an income on which they could live comfortably without doing any work—not because most men would avail themselves of the chance, but because some would, and those who did not would resent the unfairness of the others being allowed to slack. Any system of unemployment benefit is bound to have conditions attached to it: it may give a man the right to refuse some jobs without forfeiting his claim to an income from society, but it cannot give him a right to refuse to work at all. The practical question is not whether there are to be conditions, but what the conditions are to be.

The more changing the techniques of production are, and the more the economy stands in need of structural readjustments, the harder it is to define conditions which will be generally accepted as fair. A skilled man naturally resents being told that, because there are more men in his trade than are needed, he must be selected for compulsion to change over to another, in which his skill will go for little or nothing. Nor does a man who has local roots like being compulsorily transferred to some other district in which he has none, especially if there is no guarantee that he will find permanent and satisfactory employment in the area to which he is being transferred. There have, if things are to work with reasonable smoothness, to be elaborate rules regulating a man's, or a woman's, right to refuse a particular job without loss of benefit: there has to be some sort of tribunal, including some representative of the man's own class, before which he can lay his case.

When the general level of employment in a society is low, it is out of the question to devise a system of conditions that will be generally regarded as fair. At such a time, men can usually be transferred only from areas or occupations in which there is more, to areas or occupations in which there is less, unemployment. There are few occupations or areas which are suffering from an absolute shortage of workers. Consequently, transfer policies are very difficult to operate fairly, and there is serious danger that the transferred worker may soon find himself again out of a job and drift back home, so that the expense of a double removal has been incurred for nothing. On the other hand, if the general level of employment is high, some areas and occupations will be positively short of labour; and if the revival of industrial activity has been well spread, by appropriate measures to stimulate employment in the relatively depressed areas, there will be much less need for geographical, though perhaps not for occupational, transfer. It is very much easier to devise a social security system that will not either be regarded as unfair or restrict labour mobility if the general level of employment can be kept high. That, incidentally, is one reason why Sir William Beveridge rightly regards 'full employment' as a necessary assumption for the satisfactory working of his plan of social security. Proper facilities for re-training in alternative forms of skill are of course also indispensable; for men will shift their trades much more readily and be much more easily absorbed if they are given a substitute for the skill that is no longer needed in the form in which it was originally learnt.

Nevertheless there remains in some people's minds the apprehension that if the fear of unemployment is removed from the workers' minds by the double method of maintaining 'full employment'—that is, a high level of demand for labour—and social security in the form of an income guaranteed to those for whom satisfactory jobs cannot be found, the consequence will be to weaken seriously the incentives to hard and steady work during the hours of employment. Obviously, even if the receipt of benefit is made conditional, the fear of losing a job will become much less when everyone will know that he can rely on getting either another job under tolerably fair conditions or a living income for as long as he remains out of work. It is impossible to meet the general demand among the workers for greater social security without weakening those incentives to labour which depend on fear of the sack. If, however, these incentives are seriously weakened, and no new and better incentives are put in their place, what is to happen? Many employers and managers are worried about this; and it is wrong to dismiss their fears as if there were no substance behind them. The plain truth is that a community which means to be democratic, and to do what its citizens want, cannot withhold greater social security in face of the general demand for it. But neither can it give real social security without finding some substitute for the old incentive of fear of losing one's job.

One possible substitute, as we have seen, is sheer compulsion—invocation of the fear of harsh punishment instead of fear of the sack. This is the Nazi remedy; and it is clearly inconsistent with the requirements of democracy or the recognition of the rights of combination. If it is ruled out, what is left? Only the alternative of making men feel that it is up to them to do a decent day's work as an obligation which they owe to society and one which they can accept as their own. But this alternative can be made practically effective only upon certain conditions.

The first of these conditions is that men be induced to believe that their work is needed. No man, unless he possesses exceptional skill or ability, can be expected to believe this if there are a dozen idle men ready to leap into his job the moment he vacates it. Their presence is an overt sign that his work is *not* needed, and that society will be no worse off if he can get somebody to pay him an income for doing nothing. A policy of 'full employment', involving an obligation on the part of the Government to ensure that there are jobs available for all, will go a long way towards creating the psychological conditions that are needed to meet this first condition.

The second condition is that men shall feel that they are getting, on the whole, a square deal. This is in part a matter of the rules and regulations under which the social security services are administered, and in part a matter of the terms of employment. The State cannot accept the responsibility for 'full employment' without at the same time accepting a responsibility for ensuring that the jobs available are reasonably good jobs, according to current standards, A 'full employment' policy involves a public minimum wage policy, public regulation of the hours and conditions of work, reasonable welfare provisions, outlawry for blind-alley employments, and a number of other measures of industrial reform. It involves, in effect, a labour code of fair dealing, with the State as agent for its enforcement.

The third condition is not merely the recognition but the positive encouragement of working-class combination, both in Trade Unions of the traditional type and in factory groups, of which the Joint Production Committees set up in many factories during the war are the forerunners. This is involved because it is an impossible task to instil into each man individually the new attitude towards work that is called for. This attitude can arise in the required form only as a collective attitude of the working classes both in their Trade Unions and in the factory groups which represent their partnership in the tasks of production. Many men can be reached and influenced through the groups to which they belong, but in no other way. They would shut their ears to any other sort of appeal, or dismiss it as all 'blah'; but they will receive it when it comes to them as the voice of the group. This implies a new relationship in industry between manual workers, foremen and supervisors, managers and technicians; and the experience of the Soviet Union is of the greatest value where it points in this particular direction—not least significant in that it largely reproduces and amplifies the experience of those firms which, even under capitalism, have succeeded best in collaborating with their employees on friendly and confidential terms.

How much change in the ownership and control of industry will be needed in order to bring this new spirit into existence I do not propose to discuss in this book. It is another subject—one of vital importance, which I have attempted to discuss elsewhere, and shall again. Here I am concerned to point out only that this book deals with the *mechanisms* that are needed for carrying a policy of 'full employment' into effect, but that I am well aware that the effectiveness of these mechanisms will depend in practice on the spirit in which they are worked, both by administrators and managers and by the main body of the producers in every industry and service. No policy, however well devised, will work satisfactorily unless most of those who have to carry it out believe in it, want it to work, and are prepared to give of their best in making it work. At any rate, this is true within the conditions of democratic freedom. Tyrannical power, backed by brutality carried to extreme lengths, may be an alternative; but we are not called upon to consider it here.

What we must consider is to what extent we are prepared to give the achievement of 'full employment' a position of priority over other post-war economic aims. The case for doing this is very strong. It is a democratic case in the fullest sense. What the land was to the people of France in 1789 and to the peoples of Russia in 1917, economic security through steady employment is to the peoples of the capitalist countries to-day. It is not everything; but it is the thing which, amid all the welter of economic life, they have singled out. It is what they want; and it is the business of those who aspire to lead them to make sure that it is what they get.

CHAPTER I

WHAT IS UNEMPLOYMENT?

IN TIME of war, the total war which is waged by modern nations, unemployment practically ceases to exist. There are jobs for all: indeed there are everywhere more jobs than there are men and women to fill them, and those who direct the rival war machines cry out ceaselessly for more and more labour. Largely, of course, this demand is for workers to take the places of those who have been called up for service in the armed forces, and to keep the ranks of these forces continually replenished in face of war wastage. But even if there were no such drain upon the national man-power, and if wars could be actually fought by automata without the aid of human beings, the labour situation would be much the same. Each side would make the utmost effort to increase its output of these automata and of the supplies needed for keeping them in the field; and the same conditions of labour shortage would arise, more slowly perhaps, but not less certainly as the war advanced towards its decisive phase. Where nations are contending with all their might, the limit to their efforts is reached only when every person and thing that can be diverted to war production has been brought fully into use. The war-makers want all the men and women they can get, not only for the armed forces, but also for every variety of war work: they are intent on cutting down to the lowest possible point the labour and the other productive resources that must be spared to provide for the maintenance of ordinary civilian supplies. It becomes necessary, because of the shortage of resources, to do everything possible to curtail civilian consumption, subject only to the need for keeping up really indispensable services. This aim is, no doubt, seldom fully achieved; and in practice a little unemployment remains even at the height of total war. But what does remain is not due to any shortage of jobs: it is the result of misfits, temporary dislocations, or of the presence on the register of a few persons who are really unemployable. Certainly, under the conditions of modern war, unemployment ceases to be a social problem. The problem is shortage of labour, not redundance.

Why is not the same thing true in time of peace? To a certain extent it can be true, in certain countries. For some time past, there has been no unemployment problem in the Soviet Union and, at any rate in industry, there have been in that country more jobs looking for workers than workers looking for jobs. In a more limited sense, the same thing was true of Nazi Germany, for some time before the actual outbreak of war. We were told that, in Germany, this situation was due to rearmament—to the absorption of workers in the armed forces and in the economic tasks of preparation for war. We were told that, in the Soviet Union, it was due to the forced pace of industrialisation that was set by a Government determined to turn an economically backward country as speedily as possible into a thoroughly modern industrial power. We were told further that in both countries the abolition of unemployment had been purchased at a very high price—at the price of freedom. Both the Nazi and the Soviet systems were denounced as 'slave systems'; and the unemployed workers of Great Britain, and the many men who stood always on the verge of unemployment, were asked to console themselves with the thought that there was no enjoying freedom save at the expense of insecurity, and no security possible except that of the slave.

I shall not pause now to inquire whether or how far these charges were true, either about the Soviet or about the Nazi system. On that I have said a little already. What is pertinent to observe is that, in our own country, the plentiful jobs which exist in time of war are by no means all jobs at which men and women would labour of their own free will, in return for the rewards attached to them. It has become necessary on an increasing scale, as the war has advanced, to dictate to men and women where and at what they are to work, and to press compulsorily into wage-earning, as well as into the forces of the State, many who would not of their own accord have gone out to work at all. Women as well as men have been called up for compulsory service in Great Britain; and we are witnessing the spectacle of the German Nazis combing almost a whole continent for forced labour to man their factories and to till the land, and thus both to increase industrial output and to release yet more Germans for service in the armed forces of the State.

Our own experience shows us that 'full employment', if it is taken to mean the employment of everyone who is capable of serving usefully the national productive effort, involves a large measure of compulsion. It has involved this in a number of forms—compelling to work those who do not want to work, compelling people to work at one thing when they would much sooner work at another, compelling people to work in one place when they would rather work elsewhere, and compelling people to work longer hours and with fewer holidays, as well as often more intensely, than they would work if they were not compelled. Under war conditions employment is carried a long way beyond the point of abolishing what economists call *involuntary unemployment*: it extends to abolishing a great deal of *voluntary unemployment* as well.

This distinction is important. The persons we think of as unemployed in time of peace are those who are looking for jobs, but are unable to find them. We do not count among the unemployed those who are not looking for jobs. It is true that this distinction is not always easy to make. It is often argued that the unemployed registers include persons who are not really wanting to get work. This argument was used, for example, a dozen years ago as a reason for making it much harder for married women to qualify for out-of-work benefit under the State scheme. Again, a great many people are looking not for any sort of work they can get, but for work of a particular kind or under particular conditions. A skilled worker will not, if he can help it, accept work in an occupation in which his painfully acquired skill will go for nothing: a Trade Unionist will usually refuse to accept work at less than the standard rate for his trade; and a man or woman may very likely be reluctant to accept a job which means breaking up the home and migrating to a distant area, especially if there is no assurance that the job will continue for more than a short time, or if there are other members of the family who will forfeit their jobs should the head of the family be compelled to move away. There are many shades between 'involuntary' and 'voluntary' unemployment; and the point at which the line is drawn is a matter of social custom and legislative and administrative practice. Labour is not a homogeneous lump or heap of so many workers, all available for any job that is going. It consists of men and women, youths and girls, of many different kinds and degrees of skill or dexterity, and conditioned by many different personal and family circumstances. There can be no exact definition of what constitutes 'involuntary unemployment'; but in practice, interpreting the term according to our established customs, laws, and administrative rules, we have usually a pretty clear idea of what it means.

Under normal conditions, most people would agree in regarding a country as having 'full employment' when 'involuntary unemployment' in it was being kept down so low as not to constitute any serious social problem—which would mean in practice when there were very few persons who had to look for jobs long before they found them, and when the amount of 'frictional' unemployment arising in connection with workers changing over from one job to another was being kept reasonably low. No account would be taken of the number of persons who were neither employed nor looking for jobs; for this would be regarded as depending on the social structure—that is, on the numbers of persons exempt from work through the possession of unearned incomes, on the laws and customs regulating the age of entry to and retirement from employment, and on the habits of the community in respect of the 'gainful employment' of women, and especially of married women. The proportion of 'occupied' to 'unoccupied' persons—to use the Census terms—in the community depends on all these factors, as well as on the distribution of the total population by age and sex groups. But being 'unoccupied' is regarded as something essentially different from being 'unemployed'. The 'unoccupied' are those who, for one reason or another, are not seeking 'gainful employment': the 'unemployed' are those who are seeking it, but in vain.

Evidently, the proportion of occupied to unoccupied persons will vary with changes in the social system, as well as in age or sex distribution. The abolition, or severe limitation, of unearned incomes would force more people to work: the establishment of adequate old-age pensions would foster earlier retirement: the raising of the school-leaving age would reduce the supply of juvenile labour: the closer assimilation of rights and obligations between the sexes would cause more women to work outside the home, and so, probably, would an extension in the range of communally provided services. The level of unemployment, however, is to be reckoned by considering how large a proportion of those who are seeking work are out of work, whether those seeking work be many or few in relation to the total population. We need not enter here into the very complicated question whether an increase in the total numbers seeking work among a given population is likely to add to, or to diminish, the proportion unemployed. We may have to come back to that later, when we are considering what are the forces that determine or affect the level of employment.

It is, however, necessary at this point to refer briefly to a distinction which I have so far ignored. Not all 'occupied' persons in a community are 'employed', or seeking to be 'employed', in the ordinary sense of the word. Some such persons are employers, and others work 'on their own' without an employer. A jobless person who has been previously an employer or an independent worker is not usually counted as 'unemployed', though in effect he is, and though he may of course become a seeker for employment in the narrower sense. The term 'unemployment', in its commonest usage, is confined to persons who have been employed under a contract of service, at a wage or at a salary, and have fallen out of such work. Here again the line is not always easy to draw. It is especially difficult in such cases as the relatives of farmers working on farms, or persons who alternate between wage-earning and working on their own. Over a still wider field, unemployment is exceedingly difficult to measure in predominantly peasant communities, where many workers alternate between wage-earning and work on the family holding, and a scarcity of industrial employment often drives many out-of-work townspeople back to the land, where they crowd upon the peasant holdings, pressing down the standards of living, and constituting a problem which economists call by the name of 'concealed unemployment'.

Thus unemployment, as it is measured in official statistics, means different things in different countries and, even where it means much the same thing, has different significance in relation to different countries. A country in which a high proportion of the occupied population works on the land on small peasant farms may have but little unemployment that is recorded officially, and may yet have a great deal of 'concealed unemployment'. The closing of a large number of small shops, the driving of a number of small farmers out of business, or a decline in the number of persons working on their own, say, as dressmakers or independent artisans, will not be recorded as a growth of unemployment unless or until these disemployed persons become competitors for employment at a wage or salary. Official statistics in most countries take no account of unemployment among private domestic servants; and so on. If, however, we are considering the problem of 'full employment', we have to take account of these excluded groups, which may be more or less numerous according to the social and economic structure of the country concerned. 'Full employment' means, as a statement of what is to be aimed at, not only the reduction to a satisfactorily low level of the number of persons registered as unemployed, but also the full use of all the available labour, whether employed at a wage or salary or not, up to the point at which leisure is socially regarded as preferable to further labour, and within the limits set by law or custom to the 'gainful' employment of particular classes of persons—the young, the old, the ailing or partially disabled, the housewives, and the 'well-to-do'.

Indeed, 'full employment' means a good deal more than this; for it includes the utilisation of other productive resources besides human labour. It extends to the full use, in conjunction with labour, of mines and factories, land, and all sorts of capital resources that can be used in the production of goods or services. A country would not be, in any real sense, in a condition of 'full employment' if it used great quantities of labour in doing by hand jobs which could be done better and faster with the aid of machines, and had at the same time the machines standing idle and unused. This may appear a fantastic illustration; but it is in effect what happens when the State, in order to make work for the unemployed, deliberately sets them to jobs which will use up as much manual labour and as little machinery as possible, with the idea of employing a large number of persons at a low aggregate cost.

The notion of 'full employment' is, however, much harder to apply accurately to unused factories, machinery, mines, land, and other non-human productive resources than to human beings. A man or woman is usually regarded as employable as long as he or she is able-bodied, or, even in the case of partial disablement, capable of 'light work'. The availability of non-human resources cannot be measured in quite the same way. Suppose there are a number of blast-furnaces out of use. If it is decided to increase the output of pig-iron, either these disused furnaces can be brought back into use or new ones can be built. Which is the correct course will depend on a number of factors. Is the increased demand for pig-iron expected to be permanent or merely temporary? If the latter, it will probably be best to use the existing furnaces, even though they may be technically much inferior to the latest designs. On the other hand, if the increased demand is expected to last, it will probably be better to build new efficient furnaces and scrap the old ones, or at any rate a number of them. If, however, the increased demand is urgent, in the sense that the additional pig-iron is wanted quickly, it may be best to bring the old, obsolete furnaces back into production and use them until the new ones can be got ready. In wartime especially, it is often necessary to bring obsolescent plant back into use, because resources cannot be spared to build new plant, even if it would yield superior results.

There is another factor which, in existing societies, often influences the use or disuse of obsolescent resources. If new blast-furnaces are to be built, the person or firm that takes the responsibility of building them must expect to be able to recover the cost of construction over a period out of the selling price of what they produce. Selling prices must be high enough, or must be expected to be high enough over a reasonable period, to cover total costs. But this is not necessary in the case of the blast-furnaces which are already in existence; for it will pay to work them if selling prices are high enough to cover running costs, as distinct from capital costs, and to make even a small contribution towards a return on the capital already sunk in the fixed plant. Therefore, even if the efficiency of the old furnaces is much lower than that of the new, it may be financially profitable, under the existing system, to bring them back into use rather than to build new and more efficient instruments of production.

It will be realised, in the light of this illustration, how difficult it often is to say whether a closed coal-mine, or factory, or shipyard ought to be reckoned as an unemployed productive asset or not. If it is no longer fit to be brought back into use, however demand for the product may increase, it has clearly no more than a scrap value. It may, however, be very difficult to know whether conditions which will make it usable again are likely to occur; and its owners, anxious if possible to conserve a part of its capital value, beyond mere scrap value, may go on spending money on keeping it in usable condition even when the chance of its reopening has become slender. This chance depends on a complex of factors—on the difference in efficiency between it and more modern plant, on the proportions of new, fairly new, aging and obsolescent plant in the total equipment of the industry concerned, on the degree and duration of expansion to be expected in the demand for the products of the industry, and even on the financial structure of the particular business to which it belongs. Evidently, in the short run a recovery to a condition of full employment from one of depression is likely to bring a good deal of obsolescent equipment back into use. If the recovery is sustained, this old equipment will be gradually replaced by new; but the rate at which it will be replaced will be affected greatly by the degree of difference in technical efficiency, or in other words by the current rate of technical progress in the industry concerned.

These considerations make it impossible to add up the unemployed industrial equipment that exists in a country, so as to arrive at an idea of the proportion of capital resources that are lying idle. We may know how many coal-mines or factories have gone out of use over a period, and what was the value of their output when they were in use. We cannot know how many of them it would be expedient to bring back into use under conditions of full employment without a thorough survey of the technical and market possibilities in each case. The answer will, of course, depend not only on technical considerations, but also on the expected expansion of total demand for the kinds of products which the closed establishments could be used to make; and this is itself a complex matter, depending both on the varying expansibility of home demand for different products and on the prospects of export trade.

It may be said that human beings, as well as plant, can be obsolescent or obsolete as productive agents. This is obviously true, especially in the case of managers or designers who are too old or too stiff-minded to adapt themselves to changes in technique, or of skilled workers whose skill is superseded by some new invention or by a decline in demand for their products. It may not be worth while to attempt to re-train for a new job, or for new methods, a person who is not easily adaptable and is getting near the retiring age. Where this is the case, the person in question ought not to be regarded as unemployed. He ought to retire, and provision ought to be made for an adequate living pension. These cases, however, should be relatively few if proper attention were paid to keeping all grades of persons up-to-date in their several callings, and for re-training for new occupations wherever a particular skill is becoming obsolete or redundant in supply. Failure to attend to these two vitally important things is responsible for a great deal of waste and inefficiency. Few managers or workers, and even few designers or technicians, are given reasonable opportunities for keeping themselves up-to-date by refresher courses or periods of service in the most modern factories; and, except in time of war, there is practically no provision for the re-training of workers in alternative kinds of work. It is one of the best features of the Beveridge Report that it proposes to institute extensive arrangements for re-training as part of the unified Social Security Service.

In general, whereas machines should be scrapped without compunction as they become obsolete, human beings should be scrapped only in the very last resort. This is not mainly because the community needs, or should need if it were properly organised, the services of every available worker: it is even more because it is not good for men or women to be without a regular job. Above all, it is essentially bad for a person who has been used to a regular employment to be thrown on the scrap-heap as useless while there is still plenty of life and energy in him, simply because his skill has been rendered obsolete or redundant by changes in technique or in demand. If people are to be scrapped, it is of course a great deal better to provide decent pensions for them than to leave them destitute; but it is better still to provide them with the means of doing further useful work. They are happier so, and healthier: they get on better with their children and their neighbours: they stay younger, in mind as well as in body. Of course, the jobs they are re-trained for must be suitable to their age and capacities: I am not saying that *any* job is preferable to being retired. But, as long as health and strength last, a good job is for most people greatly preferable to an early retirement, even with the means of decent living assured. I say this, not as wishing to make men for as long as possible the slaves of the machine, but as holding that men have more self-respect and more happiness as active than as merely passive citizens.

If it is difficult to find any way of measuring the unemployment of industrial instruments of production, it is evidently harder still to make any measurement of unemployed land. Machines and buildings are made by men to suit their own purposes: they are made to be used—to be employed. Land, on the other hand, is not man-made, except where it is actually reclaimed from under the sea: it is at most man-improved. No community at any time makes use of all its land; for some part of its land surface is deemed unusable for any purpose. Land which has been improved for cultivation or for some other purpose, and has then been allowed to go out of use, is analogous to an unemployed factory or machine. If more land is needed it may or may not be worth bringing back into use in preference to improving waste land that has not previously been improved by human effort. In other respects, however, land differs from buildings or machines. They wear out, whereas it normally lasts for ever—though it is quite possible for its productive capacity as far as agriculture is concerned to be totally destroyed by ill-usage. How much of the available land surface any country will decide to use depends on its methods of cultivation, which determine the intensity of use, on the number of persons who can be employed more usefully on the land than in other occupations, on the quality of the land itself, on the conditions under which foreign trade is carried on and under which other countries use their land in producing agricultural surpluses, and so on. There is no presumption that all land ought to be used, for agriculture or for anything else: each community pushes its use of its land to such margins, extensive and intensive, as it thinks fit in the light of its social structure, its population, and its economic opportunities in all the various fields of production. As against this, it creates only such buildings and machines as someone in it expects to be able to make use of; and there is accordingly a presumption that buildings and machines will be used until they are either worn out or rendered obsolete by the advance of architectural or productive technique.

In view of the difficulty of measuring unemployed non-human resources, it is for most purposes a near enough approximation to the truth to measure the underemployment in a community by measuring human unemployment. This measure must, however, include the underuse as well as the absolute non-use of human resources. It must take account of intermittent or short-time working. In one industry a decline of, say, ten per cent in the volume of output will be accompanied by a nearly corresponding increase in the number of persons out of work: in another industry the smaller output will be spread over almost the same number of workers as before. Some industries—cotton manufacture, for example—work under organised short-time systems, shutting the factories for so many days a week, or for one week every so many, when demand is slack. Even in these cases there will probably be some increase in complete unemployment, as some factories will shut down altogether; but the main effect will be a shorter working week all round, with less pay. In other industries slackness of trade will be met by closing whole factories or departments or by reducing the number of machines worked, so that the total employed force will be cut down. Yet other, more casual industries, such as dock work, will employ labour more intermittently when there is a smaller total volume of work. The unemployment statistics of different countries reflect these varying forms of unemployment and underemployment in different ways. Usually, no account is taken of unemployment which does not extend beyond two, or sometimes three, days in a single week. In Great Britain, in normal times, the count of the unemployed is taken monthly, on a particular day: so that a spell of bad weather may cause a big rise in the recorded figure of unemployed builders, and in the textile trades the totals will be much affected in bad times by the number of mills that happen to be open or closed in that particular week.

The British statistics, though they take no direct account of underemployment, do in practice cover a fair proportion of it, though by no means all. It can be taken as certain that the difference between the recorded levels of unemployment in good and bad times is a good deal less than the real difference in the total volume of employment. Much underemployment escapes the count in bad times; and, of course, in good times no account is taken of overtime working, which is always prevalent when demand is brisk. Overtime may indeed exist on a large scale in some trades even when there is substantial unemployment in others, either because of a shortage of workers possessing the special skills which are in demand, or because of a shortage of the right kind of machinery or equipment and of the difficulty—real or imaginary—of introducing shift working.

The sum of the argument comes to this. Inadequate as the recorded statistics of unemployment are as a measure of the underuse of total productive capacity, we have to go mainly by them, in default of anything better. We have, however, always to bear in mind that they are seldom of much use in measuring agricultural, as distinct from industrial, underuse of capacity. There are, no doubt, figures of unemployment among farm labourers; but these usually remain low even when agriculture is declining, because there is a drift away from the land to seek for other kinds of work. Moreover, in slack times the farmer and his family for the most part become unemployed only in a 'concealed' sense. Unless and until they are actually driven off the land, they suffer a fall in standard of living rather than a loss of work. The value of their product, and probably in many cases (but not in all) the volume of physical labour done, falls off; but there is no unemployment in the ordinary sense of the word. Analogous to this is the case of the small trader who experiences a loss of custom. He hangs on to his shop as long as he can, with the result that labour is being wasted in distribution, though there is no visible rise in unemployment. The same thing happens to professionals who work for fees; and something not unlike it happens to owners and managers and permanent staffs of many businesses, who stay at their posts when trade is slack, but have less to do.

Evidently, a properly organised economy should aim at avoiding such forms of waste, as well as visible unemployment. Labour, or employment, is not an end in itself: it is primarily a means of making useful things or rendering useful services. It can be, not only for the artist in a narrow sense but for anyone who has the consciousness of doing well a job that is worth doing, in itself a pleasurable and satisfying activity; but this is not enough to erect it into an end, nor can most forms of labour have this quality continuously, for men who labour at them day after day and year after year, not omitting, as the artist commonly can, the days when they 'do not feel like it'. Most labour, even if it can give satisfaction from being useful and well done, is to be regarded as a means, not as an end; and it follows that the aim of society, in organising labour and employment, must be to get the largest possible useful product out of the least possible expenditure of productive resources. There are indeed limits to the legitimate pursuit of this aim. There is the limit set by the preference of society for more leisure to a larger volume of physical production; and there is the vitally important consideration that irksome or unhealthy or degrading forms of labour ought to be avoided wherever possible. States which enact factory laws seek to limit unhealthy forms of labour at the risk of productive loss—though in practice the effect of healthier conditions often turns out to be not loss but gain in production as well as in human welfare. There is no such objective measurement yet of irksomeness in labour as of unhealthy conditions; and it is generally left to the workers to protest against highly unpleasant or degrading labour conditions. This is often an ineffective method; for the most helpless workers gravitate towards the employments which are most irksome or degrading; and often the offer of higher pay induces even those who are not helpless to acquiesce in forms of speeding up and so-called 'scientific management' which ought to be ruled out on humane grounds. Something is done to reduce irksomeness and monotony by employers who have social consciences or realise that such conditions may be actually adverse to productive efficiency in the long run; and it is legitimate to hope that, with the advance of Industrial Psychology, more will be done to stop degrading or nerve-racking methods of production—at any rate if Industrial Psychology develops as a science and not as the biassed handmaiden of short-sighted profiteers. In a sane economic system, though employment will be regarded as a means to production, production itself will not be erected into an absolute end regardless of the wear and tear of body and spirit which it inflicts upon the producers.

Subject to these limitations, we may treat employment as a means to production; and we shall accordingly include in our conception of 'full employment' as an object of public policy the notion of employing all the available labour in such ways as will ensure the highest practicable return for each unit of effort involved. 'Full employment' means, not somehow shoving all the available workers into jobs, but getting them into the right jobs and in the right combinations with the non-human factors of production.

The great question is, how this is to be done. Is it enough for the State, through the appropriate organs, to take such steps as will ensure that, in the aggregate, there will be enough jobs to go round, and apart from that to trust to the familiar forces of supply and demand for particular kinds of labour to sort the workers out into the right jobs? Or is it necessary to go further, and to plan in such a way that jobs shall be available in the right proportions, and that the workers shall actually find their way into the jobs best suited to them? If the first solution is accepted, the role of the State is mainly monetary, supplemented by the institution of public works to fill in the gaps left by private enterprise. If the second solution is held to be necessary, the State's function becomes much more complex and extends much further—perhaps, but not necessarily, as far as a completely or preponderantly socialist, or collectivist, system of enterprise. Which is it to be?

'FULL EMPLOYMENT'—THE TRADE CYCLE

'FULL EMPLOYMENT', we are told, should be the primary aim of post-war economic policy. This doctrine, that the maintenance of employment at a high level is the main thing to aim at, and that the responsibility for it rests on the Government as the chief engineer of social welfare, has been brought into favour by Lord Keynes and his followers, and is now widely accepted among our more progressive economists. It represents, of course, a complete departure from the opinions formerly held, and commonly preached as 'economic laws', by economists of the *laissez-faire* schools. They used to assume that, under the competitive system, the level of employment could be left to look after itself, that there would be employment available for all if only no one would stand out for a higher reward than he was really worth, and that government intervention designed to create employment by such means as the undertaking of 'public works' would almost invariably do more harm than good. Everyone whose labour was worth anything at all, or at any rate every able-bodied person who looked hard enough, would be able to find someone ready to buy his labour or its product; and accordingly it was assumed that if a person was unemployed it was probably his own fault or due to some defect in him that made him simply not worth employing under any conditions. It was, of course, admitted that there could exist, even under conditions fully complying with 'economic laws', a certain amount of 'frictional unemployment', by which was meant either brief spells without work in the course of changing from one job to another, or unemployment due to the decay of certain trades or areas and to the delays involved in changing from one trade to another or in migrating from one district to another in search of work. It was even admitted that 'frictional unemployment' of this latter kind could have serious consequences for some individuals who were unlucky enough to find their skill superseded by changes in industrial technique.[1] What was denied altogether was the possibility of a situation in which there could exist, over the economic system as a whole, more workers looking for jobs than jobs to be filled. If this *seemed* to be the position, it was put down to the obstinacy of some workers in demanding more pay than they were worth; and Trade Unions were denounced as anti-social bodies because they encouraged workmen

[1] See Ricardo, *Principles of Political Economy*, Chapter XIX, for an early recognition of this truth.

to stand out for unduly high wages, and thus caused unemployment by flying in the face of 'economic laws'.

All this was said, no doubt, of an economic system resting on a basis of competition. It had to be admitted that it would not hold good under conditions of monopoly. Employers competing one with another would all be trying to sell as much as they could at any price which would allow them to cover their costs of production, and would all be competing with one another to hire labour in order to increase their output up to this point. Under these conditions, competition between employers for workers and between workers for jobs would cause wages to settle at the levels at which all the available workers could be employed—subject only to such exceptional 'frictions' as have been mentioned. But under conditions of monopoly this need not be so; for the monopolist, having no competitors to fear, would be free to pick that particular level of output and price that suited him best, in the sense of promising to yield the largest total profit. Commonly, it would suit the monopolist to stop production at a lower point than would be reached under competitive conditions, and therefore the monopolist would employ fewer workers than would have been employed if 'free' competition had prevailed. Trade Unionism was regarded as a particular kind of monopoly, holding the price of labour above its 'natural price', and thus restricting the supply.

It was admitted that unemployment in a particular industry could be caused by monopoly; but this was not held to invalidate the general doctrine, because it was assumed that monopoly would be the exception, and competition the rule. The monopolists, by employing fewer workers in the industries under their influence, would leave more to compete for employment in other occupations. But the effect of this would be, not to leave these additional workers out of jobs, but to force down wage-levels in competitive occupations, so as to enable them to absorb more labour. The workers would be worse off, and the monopolists the richer; but there would be no growth of mass-unemployment as long as the workers were not misguided enough to stand out for higher wages than would make it possible for all of them to find jobs. Economists who took this view regarded monopoly as an evil which could legitimately be combated and broken up by government action with the object of restoring competitive conditions. But they regarded it as an evil exception to a rule of competition which they thought could be relied on to hold good in the great majority of trades and occupations.

The policy known as 'trust-busting', formerly very popular in the United States, belongs to this phase of economic thought. It was directed against the exceptional man or group that got astride a particular industry or process, and extracted by that means an illegitimate profit by charging the consumer too much. 'Trust-busting' was never a successful policy, because it was seldom found practicable to defeat the monopolists without resort to measures which were regarded as interfering unduly with the freedom of ordinary business enterprise. The monopolists in practice showed great agility in evading any restrictions meant to entrap them, usually by taking advantage of the many loopholes which the law had left for fear of hampering 'legitimate' forms of enterprise.

One thing the attempts at 'trust-busting' soon showed conclusively—that monopoly was not really a question of yes or no, but one of degree. Industries were not wholly monopolistic or wholly competitive, but more or less the one or the other. It was very seldom that a monopolist controlled 100 per cent of the output of a particular thing; and, even if he had done so, he would seldom have been free from the competition of other things that could be to some extent substituted for it. A monopolist came to be thought of as anyone who controlled so large a part of a particular industry, usually at some key point, as to be in a position significantly to affect its total output or the prices of its products. It came to be realised that anyone who could do this was able to affect the demand for labour in the industry concerned, and that monopoly, in this sense, was not something exceptional, limited to a few trades, but ramified very extensively, and extended not only to the particular processes which the monopolists controlled but to all industries in which the products of these processes were required. Thus, monopoly in steel-making or oil-getting would affect all industries using steel or oil, monopoly in rubber all industries using rubber, monopoly in any primary foodstuff all industries working up this foodstuff for consumption; and of course these effects of monopoly would be passed on through all the stages of production to the ultimate consumers.

It took most economists a good deal longer to see that, as monopoly worked in this pervasive way, it would be bound to affect the total demand for labour in all occupations. For the wider its range, the more difficult would it be for all the labour displaced by it to crowd into the occupations still subject to unrestrained conditions of competition, and the lower wages would have to be in order to allow this labour to be absorbed. It was indeed clear that a point could be reached at which the remaining occupations would not be able to absorb all the available labour at any wage, however low.[1] The beautiful logical demonstration

[1] For, even if the elasticity of the demand for the products of these other

that 'involuntary unemployment' could not really exist, save in a purely 'frictional' form, collapsed when it was shown that monopoly, in some significant degree, was prevalent in most industries, and that free competition was the exception and monopoly much nearer being the rule. Economists nurtured in the school of *laissez-faire* fought hard against this conclusion, because they realised that it would open the door wide to government intervention, as well as make hay of their assumption that under 'economic law' there was a powerful tendency for every producer to get the reward he was really worth.

The conclusion was, however, irresistible; and it was made the stronger when certain economists (notably the American, Chamberlin) went on to show that a form of monopoly was increasingly prevalent even in many industries which seemed to have kept their essentially competitive character. Chamberlin coined a phrase, 'monopolistic competition', to describe what happens in these cases. A number of firms are competitors in producing, say, motor-cars or vacuum-cleaners. Each firm is concerned not only to produce its wares at a competitive price, in relation to quality, but also to make its products appear different from those of its rivals, in order to build up a 'goodwill' preference for its goods over theirs. This is done partly by advertising and canvassing and various other sales devices, and partly by accumulating gadgets and seeking variety for its own sake, often at the expense of real convenience, as it makes repairs and replacements more difficult. Inevitably, all these ways of pursuing variety add to costs, and check the development of standardisation. They thus cause the competition between firms to raise prices instead of driving them down; and the higher prices mean that fewer goods can be sold, and thus react adversely on employment.

Between them, these two forms of monopoly—monopoly in the ordinary sense and 'monopolistic competition'—cover directly or indirectly a very large part of the field of modern industry. The straight type of monopoly is most prevalent in the sphere of materials and of half-manufactured goods, such as steel, and spreads its effects from this sphere into the finishing processes, inflating prices and reducing output all along the line; whereas monopolistic competition prevails most in the sphere of finished consumers' goods and in that of machinery, and reacts most on the costs of selling and distribution.

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industries was at the outset high, as more and more labour crowded into them elasticity would be bound to fall, until they could absorb no more labour at *any* wage.

In face of so widespread a system of monopolies, each incomplete in itself, but each strong enough to affect markedly the conditions of production and sale, it is the veriest nonsense to contend that the traditional picture of an economic order tending, through competition, to employ all the available resources of production and to assign to each 'factor' its appropriate economic reward bears any significant resemblance to what happens in the real world. It is a plain fact, visible to anyone who cares to look, that in the real world the available resources are usually by no means all employed, and that the unemployment which exists cannot plausibly be explained as the result of 'friction' in changing from job to job or even of friction due to technical changes. These causes are no doubt responsible for some of the unemployment; but there are other, and even more powerful, forces at work to drive total employment below the level that is needed if we are to make the most of our economic resources in abolishing want and raising our standards of living to the highest point compatible with our technical mastery of the arts of production.

Of course, all economists, no matter to what school of thought they belong, are bound to admit that this waste of productive power exists. It exists, however, they point out quite truly, on a much larger scale at some times than at others. There is, in effect, a something which they call the 'trade cycle', which brings it about that economic activity ebbs and flows, not indeed with a rhythm as regular as that of the tides, but regularly enough to suggest that there is some single and definable cause at work. This alternation of high and low economic activity, we are told, can be traced back right through the nineteenth century, and even right through the eighteenth—though naturally the statistical basis gets narrower the further one attempts to follow it back. There are no statistics of unemployment going back beyond 1850; and even those for the second half of the nineteenth century are very imperfect. Production figures are available, for a few kinds of goods, over a longer period; and so are figures showing the average trend of prices for a larger number of goods. Altogether, there is enough statistical evidence to reveal a fairly clear up and down rhythm of total economic activity in Great Britain for nearly a couple of hundred years back, and for other industrial countries as far back as the statistics allow us to go. The length of the different cycles has varied from about seven to about a dozen years; and every now and then wars have upset the movement. But its existence is not open to doubt; and we could not indeed doubt it even if there were no statistics at all, for we could tell from newspapers and from other contemporary sources that this was on the whole a good and this a bad year, and could construct a picture of the fluctuations of economic activity (as I have actually done) without making use of any figures at all.

Economists who claim that a *laissez-faire* system has a tendency to bring about the employment of all the available productive resources at prices (or rewards) appropriate to their several services to production admit that this tendency is again and again upset by the working of the 'trade cycle'. Intent on preserving their faith in the beneficent tendency of the system, they then attempt to explain the 'trade cycle' as due to some external or particular force impinging upon it and causing it to work amiss. Some economists have attempted to explain this up-and-down behaviour of the economic system mainly in psychological terms, as due to the alternating errors of optimism and pessimism made by business men in the mass. Others have tried to trace it to variations in crop-yields, affecting the agricultural and through them the industrial producers. But by much the commonest of these explanations is that the trade cycle is basically a 'monetary phenomenon' and is essentially due to the imperfect or foolish management of the supply of money. Money, in any developed economic society, is a necessary instrument for bringing about the easy exchange of goods and services. It is immensely superior in convenience to the barter of goods for goods, because money is a 'universal equivalent', and whoever possesses it can exchange it for any kind of goods or services that are on the market. But with this convenience money, we are told, has the disadvantage that it can easily be managed or manipulated in such ways as to disorder the entire economic system and to cause crisis and mass-unemployment.

Money, in these explanations, is always represented as something apart from the underlying character of the economic system, which consists fundamentally of exchanges between real goods and services. Money was invented in order to facilitate these real exchanges; but in achieving this it somehow gets out of hand and develops, most inconveniently, a 'behaviour' of its own. Economists sometimes speak as if this untoward 'behaviour' of money had come into being only with the development of modern banking—with the power of the bankers to create money out of nothing by printing banknotes or, more recently, by simply creating bank deposits against which cheques can be drawn. But there is ample evidence that money 'behaved' inconveniently long before the development of modern banking techniques, and when most money was still made of materials, such as gold and silver, which possessed a value and uses of their own, quite apart from their use as means of exchange. If money is the factor which is responsible for upsetting the economic apple-cart, the blame must be attributed not exclusively to the methods of the bankers in the modern world, but also to the solider kinds of money which are often praised for their intrinsic worth as against the merely 'token' character of modern bank money. The inflow of gold and silver into Europe from the New World in the sixteenth and seventeenth centuries was quite as upsetting an event as the development of country banknotes at the time of the Industrial Revolution or the adoption of the cheque and deposit system in the course of the nineteenth century.

Money is in effect essentially unstable. It is unstable because, where it is made out of the precious metals, the supply of these metals varies both with the discovery of new sources of supply and with technical changes in the conditions of mining, and because, where it is made out of paper or by mere book-entries in bank ledgers, the conditions under which the law allows it to be made vary, and so do the conditions under which bankers, following rules of their own making, see fit to create it, or to annihilate it after creating it. Most bank-money, except in times of emergency, is supposed to have some sort of backing in a stock of precious metal held by the banking system, or by the State; but the amount of paper-money, or of bank deposits, that can be created against a given reserve of the precious metals varies by law and custom from time to time and from place to place. So does the amount of bank deposits that can be created against a given reserve of currency, including paper notes. People's habits in using money also vary; and money changes hands much more rapidly under some conditions than under others and, in accordance with the rapidity or slowness of its circulation, does more or less work in facilitating the exchange of goods and services.

Why, from the standpoint of its effects on economic activity, does the amount of money, or the rapidity of its circulation, matter? These things matter because they affect the prices at which goods and services are bought and sold, and because prices react on the volume of economic activity and of employment. How the supply of money affects prices is not at all easy to explain, beyond the broadest generalities; but it is an unquestionable fact that in most circumstances a large increase in the supply of money will have the effect of increasing the prices of many kinds of goods and services, if not of all. If people have bigger incomes, they are prepared to pay higher prices than they otherwise would; and if the supply of money rises faster than the supply of things to be bought, each unit of goods and services will tend, except where its price is fixed by law or contract, to fetch a higher price. How much higher, is another matter; for we cannot say that a rise of x per cent in the supply of money will cause a corresponding rise in average prices—nor could we, even if the supply of goods and services were to remain unaffected, as in practice it never does. There are far too many complications for any such precision to be possible. Money can pass from hand to hand faster or more slowly; and this will affect, as we have seen, the amount of work a unit of money does in a given time, and therewith its influence on prices. Moreover, goods and services also, including second-hand goods already in existence as well as goods produced currently, can change hands more or less rapidly, or can pass through more or fewer hands on their way to the consumers; and changes in the conditions of circulation of goods as well as of money will affect prices.

It can, however, safely be asserted that, whenever the effective supply of money is increased faster than the supply of things to be exchanged, there will be a tendency for prices to rise. But there need be no such tendency, though there may be, where the supply of things to be bought and sold rises as fast as the supply of money. This may happen, for example, where there are large quantities of unemployed economic resources which can be brought into productive operation under the stimulus of the increased supply of purchasing power. In practice, however, prices will usually rise, even under such conditions; for in periods of heavy unemployment many prices are usually brought down to a low level, and employers seize the opportunity presented by a rise in incomes to ask more for their goods. Workers also, who have had their wages reduced during a slump, make what speed they can to ask for increases as employment becomes more plentiful; and higher money wages usually mean—at any rate in the short run—higher money costs of production, which tend to be passed on in higher prices. Therefore, even if the supply of goods and services increases as fast as the supply of money, prices usually rise; and the fact that they do rise thereupon creates a demand for yet more money in order to finance the sale of more goods at higher prices than before.

It is sometimes said that, though the supply of goods and services will tend to increase as more money is made available, up to the point at which there are no more productive resources that can be brought into use, there will be a tendency for prices to rise because the reserve of unemployed labour and other resources will be on the whole less efficient than the productive agents which were already in use, and costs will accordingly rise as more of them are brought into employment. This tendency has, however, to be set against another; for in many productive plants which were being used, but not fully used, until the supply of purchasing power was increased, costs of production will tend to fall as the plants are enabled to work up to capacity. This may be a very important factor in big establishments, which have large standing charges that do not vary much with the volume of current production; for when plants are working up to their full capacity these charges can be spread over a larger output and are thus smaller for each unit produced. It is true that costs will tend to rise again if output is expanded still further in these plants; for in general there is for every factory an *optimum* rate of output, at which goods can be turned out at lowest unit cost. Beyond this point, the higher costs of overtime working and the straining of the productive resources beyond what they were designed to meet tends to raise the costs of production. This is a cause of varying cost quite distinct from the changes in money earnings referred to in the previous paragraph.

The general conclusion to be drawn is that, where total production has been at a low level, so that there have been large productive resources unemployed or underemployed, the average *real* costs of production per unit (in terms of the amounts of labour and other resources used up in making them) are likely to fall for some time as total output is increased, and to begin to rise again only when the more efficient agents of production have become fully employed. As against this, average *money* costs will tend to rise from the outset owing to the pressure for increased wages, and prices will also tend to be driven up by the pressure of employers for a more satisfactory reward. These effects on *average* real costs will, however, not necessarily coincide with the movement of costs at the *margin* of production, that is, of the costs of the least efficient producers who are able to hold their place in the market. If, simultaneously, on an expansion of demand, some firms increase their output at falling costs whereas others increase theirs at rising costs, and the output of both groups is needed to meet the demand of the market even at prices which will be remunerative to the higher-cost producers, prices for the whole output will tend to rise to the level corresponding to the higher costs, and the effect of the lower costs of certain firms will be, not to reduce prices, but to present these firms with 'windfall' profits.

The total result of these conflicting forces will depend on circumstances. If the producers with falling costs can meet the entire expansion of demand, there will be no tendency for prices to rise on account of the higher costs of the marginal firms, and the high-cost producers will not be able to expand their production. Thus, what happens will depend on the conditions of supply at any particular time and place; and no absolutely general conclusion can be laid down.

It is, however, certain that the increased purchasing power made available will react in different degrees of strength on different classes of goods and services. When people have more money to spend, they do not spread their additional purchases evenly over all classes of things. Their demand for some things is much more elastic than for others. Accordingly, the increased purchasing power will produce much more effect on some industries than on others, and there may be some on which it hardly reacts at all. Moreover, the effects of increasing demand on costs will differ greatly from industry to industry. Some industries, having large unused resources that can be called into play, will be able to expand their output much more easily and rapidly than others; and some industries will experience falling unit costs, while in others these costs will tend to rise. Prices, therefore, will by no means move uniformly for all kinds of goods and services. There will be divergent movements, and even movements in the same direction will not be the same in speed or in amount. Nor should it be overlooked that a rise in total purchasing power will react quite differently on demand according to its distribution among the people. If the rise goes mainly to the very poor, it will be spent differently from the way it will be spent if it is diffused over all classes; and if it goes mainly to the wealthier members of the community, yet another effect on demand will follow. The results on prices will thus vary both according to the effect of the increased purchasing power on the structure of demand and according to the effect of the increased demand on the structure of both real and money costs.

In general, it is pretty safe to conclude that, well before the economy reaches the point of having its available productive resources fully employed, there will have been such increases in the prices of a number of goods and services as will have set in motion a demand for yet more money, in order to enable more goods and services to be bought and sold at a higher average price-level. If this demand is met, it will almost certainly lead to a further rise in prices, and therewith to a further demand for an increase in the supply of money, and so on, in an endless series. This is the process known as 'inflation'; and a good many economists are so afraid of it as to argue that the supply of money ought not under any circumstances to be increased. Money, say these economists, should be fixed in quantity absolutely, or at all events should be allowed to vary only with the size of the population, and should be fixed absolutely per head.

What is indeed clear is that, when the available productive resources are already fully employed, so that an increased supply of money can have no effect in calling additional resources into use, there can be no good reason for adding to the supply of money; for in such circumstances a larger supply can only inflate prices without increasing the output of real wealth. But it does not follow from this that there is no advantage in issuing more money at a time when there are idle productive resources ready to be called into use. The economists who live in terror of inflation will answer that the correct course in such circumstances is to keep the supply of money fixed, and to wait for prices to be reduced so that all productive resources can be employed at a lower price-level—for, as they correctly point out, any amount of money can be used to exchange any amount of goods and services if only the prices are rightly adjusted. In practice, however, this will never happen. Many employers, instead of cutting down their prices to the requisite levels, will discharge workers and reduce output in the hope of keeping prices up; and there will be many prices fixed by law or long-term contract which cannot be reduced for a considerable period. Consequently, a refusal to expand the supply of money to re-employ idle resources leads, not to an all-round fall in prices that enables all these resources to be brought back into use, but to continuing depression and to a severe upsetting of the relative prices of different kinds of goods and services. The groups which are strategically well placed for holding up the prices of what they have to sell, or are protected by long-term contracts, improve their relative position: the rest suffer. Unemployment remains uncured.

Accordingly, nothing seems to be left of the arguments advanced by the advocates of a fixed supply of money except the truism that, when all productive resources are already employed, there is no point in issuing more money in order to bring more resources into employment. We cannot, however, leave the matter quite at that; for the danger of inflation which these economists have pointed out is a real danger, and it is true that every additional issue of money which is made for the purpose of calling additional productive resources into use does tend to create a further demand for money to finance the exchange of goods and services at higher prices. This danger is obviously at its greatest when the quantity of idle labour and other resources waiting to be brought into use has already been reduced to such a point that what is left unused is markedly less efficient than what has been already absorbed in production. For at this point further absorption must mean higher real costs.

It is relevant at this point to draw special attention to the elementary economic principle that under the existing system prices tend to be fixed at the margin—in the sense that the price of a commodity tends to be that at which the highest-cost units included in the total supply can be profitably sold. This principle is subject in practice to a great many qualifications; but it is broadly true that the more efficient producers tend to reap a special profit by selling at prices determined by the costs of their less efficient competitors whose output is also needed to meet the total requirements of the market. To some extent these less efficient producers are always being crushed out by their more efficient rivals; but this seldom leads to a complete standardisation of efficiency. There are nearly always firms of varying efficiency in a trade; and as long as the output of the more efficient is not large enough to meet the total demand, less efficient firms can not only maintain themselves but, by keeping up prices, help to present their rivals with high profits. Indeed, quite often where a big firm or combine could quite easily crush out all its competitors and capture the entire trade, it prefers not to do so, because their disappearance would mean greater pressure on it to reduce its prices to a level corresponding to its lower costs of production.

As unused resources are called into play, there is, as we have seen, a tendency for efficiency *at the margin* to decline—or, what is the same thing, for real costs at the margin to increase. This is a principal factor in causing prices to rise as additional resources are brought into use. Accordingly, the question arises whether, in order to avoid or at any rate limit this tendency, it may not be preferable to leave a substantial proportion of the less efficient productive resources unused. In other words, some economists hold that a fairly high level of unemployment is positively desirable as a means of keeping prices down. This view partly explains the toleration of mass-unemployment which characterises much economic thinking under capitalist conditions. Nor is this all; for among the prices which can be kept down by the existence of unemployment is the price of labour-power. Employers, as well as economists, are well aware of this; and I have often heard employers argue that the existence of an adequate 'reserve of labour'—that is, of unemployed workers—is necessary in order to preserve factory discipline and to prevent the Trade Unions from getting out of hand.

Among economists, the argument often takes a somewhat different form. We have seen that, as the volume of employment increases, pressure for higher wages becomes much stronger and comes to be a force impelling prices to rise. What effect, ask the economists, would the virtual abolition of unemployment, or its reduction to a negligible amount, have on the terms of the wage-bargain? If every workman knew he could easily get another job, and every employer knew that he could get additional labour only by attracting workers away from other employers, would not wages rise so sharply as to lead straight to inflation? The experience of labour shortage under war conditions adds point to this argument; for everyone knows that if employers had been left free to entice away one another's employees by the offer of higher wages, there would have been a very much greater increase in working-class money incomes during the present war than has actually occurred. Indeed, the severe restrictions imposed on labour mobility and the prohibition laid upon employers in this respect were designed to prevent a dangerously inflationary situation from arising.

In wartime, it is evidently necessary to prevent such a situation; for the first essential under war conditions is to restrict unnecessary civilian consumption in order to divert to war use the largest practicable proportion of the national output, subject to the need for ensuring the requisite minimum of necessary civilian supplies. But, in peace-time, would it be a bad thing if the workers, by virtue of the demand for labour being in excess of the supply, were enabled to push up wages to a higher level, and to get a bit of their own back at the expense of other classes? In many respects it would be a good thing; but there are difficulties. In the first place, the rising costs of living would react disastrously on all persons who live on small fixed incomes—from the *rentier* members of the middle classes to the recipients of all kinds of pensions and allowances and annuities of fixed amount. The State could no doubt by legislation increase the sums paid to its own pensioners and to the various classes of beneficiaries under the social insurance schemes. But even if this were done, there would be thousands upon thousands of hard cases of private pensioners, old people living on annuities or on the interest on small savings, persons in receipt of incomes from fixed charitable or educational endowments, and so on. These classes had to encounter ruin in a number of European countries as a result of inflation after the last war; and the social consequences were neither just nor pleasant.

Secondly, inflation benefits not only the wage-earners, but the profit-makers as well. A situation in which every owner of a factory could rely on being able to sell at a high price everything he could produce would lead to a vast amount of profiteering. The shares in the total national income accruing to profits and wages would rise at the expense of the shares accruing to other forms of income. In the case of the wage-earners, a part of the increase would go in wages paid to those who were previously out of work, and a part in higher earnings to those who were already in work. In the case of the profit-makers, by far the largest gains would accrue to the owners of the more efficient instruments of production. If Trade Unionism were strong and vigorous in action, the share in the national income going to labour would probably increase at the expense of the share accruing to capital as a whole. But this is not certain: what is certain is that the share accruing to profit, as distinct from interest (and, in the short run, rent) would increase very much. In the long run, the position would be redressed, no doubt, when the community had settled down to the new conditions. But the long run would be very long; and, as Lord Keynes has wisely said, 'in the long run we are all dead'.

What has been said in the preceding paragraphs involves, of course, the assumption that the state of 'full employment' postulated in it has been reached under a system of 'private enterprise', and that the various parties to the work of production have been left free to scramble for what they can get. It has also been assumed that the prices of goods and services have been left to be settled by the interplay of supply and demand. It is obvious that, unless these assumptions are made, the conclusions do not follow. They would not, for example, hold good in a Socialist economy, in which presumably both incomes and prices would be regulated in accordance with public conceptions of the general interest. Under such a system, it would not follow that an addition to the supply of money would raise prices or set afoot movements for higher wages, as long as the output of goods and services rose *pari passu* with the supply of money. Indeed, the entire argument presented in the preceding pages would be inapplicable; for if the State were in direct control of the means of stimulating employment by simply ordering work of various kinds to be done, there would be no need for it to go roundabout and to make use of an addition to the supply of money *as a means of adding to the volume of employment*. The supply of money would follow upon, and not precede, the decisions about productive activity; and money would be made available in the quantity deemed necessary for financing the approved volume of productive operations. The rôle of money, which in a profit-seeking, capitalist economy is of primary importance as a means of stimulating economic activity, would become secondary; and monetary management would become a comparatively simple matter, following upon decisions taken in the field of production. Money would be brought back to its proper function of facilitating exchanges: it would play no part in determining the volume of production or employment.

We are, however, for the time being considering not Socialism, but what would happen if 'full employment' were to be achieved under a system of private capitalist enterprise. What would happen under a complete system of Socialism is sufficiently apparent from the Russian example; and we shall have to consider later what would happen under a 'half-and-half' system, within which collective and private enterprises existed side by side, each occupying a considerable part of the field of production. What has been said so far applies only to an economy in which, even if there exists, as there did in Great Britain in 1939, a small 'socialised sector', the greater part of the field is occupied by capitalist businesses carried on under the stimulus of the profit motive.

It may appear that throughout this discussion I have been burking the really essential issue. Are the economists who maintain that the occurrence of mass-unemployment is due to the 'trade cycle' and that the 'trade cycle' is due to the instability of the money factor in our economic affairs, really in the right? Or has the 'trade cycle' some quite different cause? I shall not waste time discussing either the attempted explanations of the 'trade cycle' in terms of harvest fluctuations or the various purely psychological theories which have been advanced. It is enough to say that nobody, I think, now believes in the 'harvest' explanation, and that, though it can be agreed that fluctuations in business 'confidence' have a powerful direct influence on the volume of employment, it seems too much to believe that these fluctuations in 'confidence' are themselves causeless, or that the mass psychology of the business world oscillates quite irrationally according to a regular rhythm between errors of optimism and pessimism. It is surely more reasonable to suppose that these alternations are the reflections of real changes in the prospects of profit. They may be, and doubtless often are, carried a long way further than the circumstances really warrant; and the proneness of business men to overestimate the strength of real forces making for boom or slump is often a potent force in causing economic fluctuations to be greater than they would be otherwise. But this does not make the causes of boom and slump psychological causes: it means only that, the jumpier business men are, the further the economic system is likely to be carried out of boom into depression, and out of depression into boom. It is perfectly true that the real causes of the ebb and flow of economic activity operate on the level of employment by being translated into decisions in the minds of business men—decisions to produce or not to produce, to engage or to sack workers, to build up stocks of goods or to let stocks run down. It is also true that of all the persons whose optimism or pessimism, without being the cause, affects the amplitude of the 'trade cycle' the bankers occupy the key positions, because their decisions determine the supply and availability of money to the producers and traders. At this point the psychological and the monetary explanations run together; and to the extent to which the bankers are actuated by alternating moods of optimism and pessimism they can be said to be positive agents in causing an advance or a decline in economic activity—though, as we shall see, it is very much easier for bankers to bring about a slump than to put an end to it. On the main issue, however, the bankers, in settling the direction of monetary policy, are usually moved much less by optimism or pessimism than by an implicit faith in certain 'rules of the game'. Most of them have deep in their minds a belief in the truth of orthodox, classical economic doctrines; and they act, as far as they can and dare, by the rules laid down for them by the classical monetary theorists. These rules tell them that it is their duty above all else to safeguard gold reserves, or, where this cannot be done, to preserve the stability of exchange rates between the money of their own country and that of countries which have ample gold reserves. Any threat to this sort of stability alarms them much more than a threat to the stability of employment or production: they respond to it by restricting the supply of money and credit, and, when the result is seen in spreading unemployment and distress, they tell the world that all will be well again as soon as incomes and prices have been brought down to a level which will correspond to the supply of money dictated by the necessities of stable rates of exchange. When this fails to happen, they blame not themselves for causing depression, but other people—especially the Trade Unions—for refusing to agree to the required reductions of income.

True, the bankers have not been able in recent years to act fully on these principles of financial austerity. (The austerity, by the way, is mostly for others; for the banks are usually well able to maintain their dividends, however the rest of the world may fare). Bankers have, under pressure from public opinion and from Governments unable to face the consequences of financial orthodoxy, considerably modified their practice; but it is much to be doubted whether they have changed their principles. Most bankers, it appears, still regard the 'rules of the game', even if they dare no longer observe them, with the same veneration as before. We shall have to watch them carefully lest, at the end of this war, they repeat successfully the attempt they made after 1918 to force the world back into the shackles of orthodox, gold-standard finance. We shall have especially to watch the Americans; for the so-called 'White Plan' issued early in 1943 from the United States Treasury dangerously foreshadowed just such an attempt.[1]

Before, however, we accept in full the conclusion that the 'trade cycle' is 'purely a monetary phenomenon', due to the inherent instability of money under the arrangements which at present govern its supply, we must pay some attention to an alternative explanation that cannot be dismissed so lightly as the others. In Great Britain, this explanation has been chiefly associated with the name of J. A. Hobson, though further back it owes a good deal to Karl Marx. Briefly, Hobson sought to trace the recurring phases of economic depression to a maldistribution of incomes which led to 'underconsumption' and therewith to a decline in production and employment. The poorer sections of the community, Hobson argued, have to spend most of their incomes on consumers' goods and services: the richer do not. The richer classes save much more than the poorer, and out of their savings come the resources which are embodied in new investment in capital goods—that is, in means of production as distinct from goods or services destined for immediate consumption. Capital goods, however, are useful, and can be profitably operated, only if there is a market for the consumers' goods which they can be used to make; for in the last resort all production leads to consumption and has consumption as its end. But the demand for consumers' goods depends primarily on the purchasing power in the hands of the poorer people; and an increase in the purchasing power going to rich people will do little to swell this demand, because the rich will save a high proportion of it. If, then, incomes are distributed with gross inequality, the demand for consumers' goods will be low; and accordingly, when the rich invest heavily in capital goods with the aim of making more consumers' goods, the additional consumers' goods coming on the market will cause a glut. The newer instruments of production, being in general more efficient, owing to technical progress, than those previously in existence, will force down prices in order to find a market in face of the limited demand. The older capital goods will be driven out of production: there will be widespread bankruptcies and failures and many workers will be flung out of work. The new capital goods will use less labour for each unit of output than the old, and will therefore not need the services of nearly all the discharged workers. Soon the rich investors will take fright, as the difficulty of driving yet more of the older instruments out of business increases. They will thereupon refuse to go on investing their savings in further capital goods for which there seems to be no demand. Producers of capital goods as well

[1] See page 143.

as of consumers' goods will then be thrown out of work; and a general depression will set in.

Before we examine the validity of this explanation, let us consider a vital point which, so far, it does not explain at all. If these are the causes of depression, what are the causes of the ensuing recovery? The trade cycle has its 'ups' as well as its 'downs'. We seem to have here a plausible explanation of the 'downs', but what about the 'ups'? Hobson's answer on this issue is much less clear. It is, partly, that, when depression has come about, the *share* of the national income going to the poorer classes, and the *proportion* of it consumed, does usually become larger, though the total income becomes smaller; and that this relative expansion of demand for consumers' goods after a time sets in motion the forces leading to a recovery. It is also, partly, that after a time the stocks of goods piled up at the beginning of the depression become exhausted; so that a demand sets in for goods for re-stocking over and above the level of current demand, which is itself increased because it can no longer be met by reducing stocks. And it is also partly, and I think more fundamentally in Hobson's mind, that there is in any scientifically impelled economic system an inherent tendency to recovery, based on new inventions which create new wants or new means of satisfying old wants. During the depression these opportunities for profitable investment pile up for a time unused; but after a time capitalists, feeling sure that the new and more efficient instruments can be operated profitably by virtue of their superior efficiency and aware that they can be installed most cheaply while prices and production costs are low, begin to venture back into investment, re-employ the producers of capital goods, and thus set on foot an expansion of the demand for consumers' goods which presently brings their producers also back into jobs. And then, of course, in Hobson's view, the whole process starts all over again. Rich men get too large a proportion of the national income; and save too much of it: underconsumption due to the maldistribution of incomes is renewed: the slump recurs.

How far is this dual explanation true? We must now go back to consider how far Hobson is right about the cause of slumps; for this is the key point of his whole theory.

CHAPTER III

SAVINGS AND INVESTMENT

HOBSON'S CONTENTION, we have seen, is that economic depressions are due mainly to a bad distribution of incomes—bad in the sense that too much is given to the few, and too little to the many. Why is such a distribution bad? Morally, it is bad because it bears no correspondence to men's wants or needs, and because it is bad for human creatures to be deprived of what is necessary for a rounded and satisfactory way of life. This argument can be cast into an economic mould by saying that the more evenly the available income of a community is divided up, the greater aggregate satisfaction it will be likely to yield. As men on the whole satisfy first their most urgent wants, the smaller incomes tend to yield, unit for unit, a larger satisfaction than the bigger incomes, because the overplus is used to meet less urgent wants. This, however, is not in the present connection Hobson's point. What he is arguing is that a grossly unequal distribution of incomes will not only be morally wrong and economically disadvantageous in yielding a smaller aggregate of satisfaction, but will also, by causing depression and unemployment, reduce the size of the total national income below what it could be on the basis of the available resources of production.

Hobson bases this contention on the assertion that, whereas poor people consume most of their incomes, rich people save a considerable part of theirs. This can be accepted as broadly true, though in fact the largest volume of saving in recent times in Great Britain has come not directly from the very rich, but rather from the middle classes and from the accumulation of reserves by joint stock companies and other corporate bodies. This does not really affect Hobson's argument, which is in effect that under the capitalist system there is a tendency towards over-saving. Too small a proportion of the national income, at any rate in times of business activity, is spent on consumable goods and services: too large a proportion is saved. As the demand for all classes of goods, including capital goods, depends finally on the level of consumption, the result is crisis, leading to unemployment and depression.

How well I remember the chorus of shocked disapprobation with which the great majority of economists greeted this argument when I was young. I was warned against it again and again; and for a long time my adherence to Hobson's point of view made me feel like an economic leper. The orthodox argument against Hobson used to be that it did not matter from the standpoint of demand and employment whether incomes were spent on consumable goods and services or on capital goods. Money invested, equally with money spent on consumption, created employment; and the persons employed in making capital goods were just as good customers of the industries making consumers' goods as anyone else. The idea that there could be such a thing as 'over-investment'—the correlative of 'underconsumption'—was scouted. More and more investment would lead, with advancing techniques, to more and cheaper production, and accordingly to a rise in real incomes all round as prices fell. The higher the proportion of the national income invested, the more rapidly would the standard of living rise. Thrift was a virtue—perhaps the first of virtues. As for the argument that the new and more efficient instruments of production would be continually driving the older instruments out of business, and thus ruining the owners and displacing the workers employed upon them, what could be better? It was of the essence of progress that obsolete capital goods should be continually displaced; and the disemployed workers, if only they would not be so foolish as to stand out for unreasonable wages or conditions, would soon find new jobs as industry expanded under the stimulus of technical advance.

Hobson, in fact, and those who agreed with him had committed a cardinal sin, for which there could be no forgiveness. They had cast doubt on the sovereign virtue of thrift: they had suggested that it was possible for a community to be too thrifty—to save too much. Such a view outraged the nineteenth-century conscience: it was not so much argued about as dismissed as rank blasphemy. It took the experience of the last war and of the chaos which followed it to make the minds of more than a few heretics ready to receive so devastating an idea; and when the economists did begin to receive it, they refused to swallow it unless it was well coated with non-Hobsonian language. Keynes sugar-coated it for the new generation of economists by wrapping it up in a new terminology difficult enough for them to have to study it seriously; and when this had been done, they began to come round to the new view—always provided that it was not attributed to Hobson. The new school became Keynesian, not Hobsonian; and a few old Hobsonians, including myself, had many good laughs when their juniors set to work to expound to them, in Keynesian language, something closely akin to what they had been denouncing as nonsense when it had only Hobson's—or Marx's—authority behind it.

There was this much of excuse for the new Keynesians' habit of brushing Hobson impatiently aside—that in certain respects Keynes undoubtedly cleared up errors and ambiguities in Hobson's argument. Hobson, at any rate in most of his writings, had appeared to assume that if an individual *saved* any part of his income, what he *saved* somehow got itself *invested* in new instruments of production. He drew no distinction—at all events no clear distinction—between the act of *saving* and the act of *investment.*[1]

[1] Such a distinction was in fact implied, though not stated, in Hobson's

These are, however, quite distinct and separate acts. The individual who merely saves merely abstains from spending. He can put his money in a safe, or in a hole in the ground, or leave it in his current account at a bank. In order that it may be invested as well as saved, he must either himself spend it on new capital goods, or transfer its use to someone who will spend it on new capital goods. If he uses it to buy *existing* stocks or shares, that does not amount in reality to investing it, but only to transferring it to the previous owner of these stocks or shares, who may then invest it or not invest it at his pleasure. From the standpoint of its social effect, saved money is not invested until it has been locked up in *new* capital assets other than money, either by being borrowed by someone who spends it in this way, or by being spent in this way directly by its possessor. There is, however, no necessary correspondence between the sums of money which persons wish to save out of their incomes or companies to pass over into their unexpended reserve funds and the sums of money which active capitalists wish to borrow or to get control of in the form of shares for the purpose of spending them on capital goods. Savers may want to save more or less than capitalists wish to spend in this way. Keynes, in his first exposition of his revised version of Hobson's thesis, put this statement in the form of saying that 'Savings' and 'Investment' are quite different things, and that there is no necessity for them to be equal.

In his later expositions Keynes, unfortunately as I think, has altered his terminology, and has created much confusion by stating that 'Savings' always under all circumstances are and must be equal to 'Investment'. It is important to understand that this apparent contradiction represents not a change of view, but merely a change of terminology. In his later statement, Keynes is looking at the problem from the standpoint of the total social effect, whereas in his earlier statement he was regarding it primarily from the standpoint of the various individuals or business concerns which either save money or invest it in capital goods. The amounts of money which are invested in capital goods may be, in the first instance, either greater or smaller than the money savings which individuals or business concerns make out of their incomes; but, whatever this relation may be, the real savings of the community consist only of the capital goods that are added to the national supply of such things. Savings which do not result in additions to the supply of capital goods are not, from the standpoint of the community, *real* savings: they are, in a phrase used by Keynes, in effect "spilt on the ground". They

theory; for in the crisis the capitalists were represented as refusing to continue to invest in new capital goods.

must be; for they have resulted in an addition to the supply neither of capital nor of consumers' goods nor of services. They represent no real wealth at all.

This, of course, is not apparent to the individual saver. He has saved his money, and he still has it, either in cash or in bank deposits or in the second-hand stocks or shares he has bought with it. Why, then, is it not real saving from the standpoint of society as a whole? Because, when more money is saved in these ways than anyone is prepared to make use of for the purchase of currently produced capital goods, the result must be to inflict an equivalent loss on other people. Under conditions of what economists call 'equilibrium', the total sum paid out in incomes to the members of the community should be just enough to buy the whole of the current output at prices which will cover the costs of production, including normal profits (which economists usually include as an element in cost). If some part of the income thus paid out is not spent at all in buying current products, either capital goods or consumers' goods and services, the incomes that are spent on such things will clearly not suffice to buy the whole current output at prices which will cover its cost. Either some of the current output will have to remain unsold, and its owners will therefore lose both by the cost of holding it in stock and by drawing no income from the capital locked up in it; or all the current output will have to be sold at less than cost, so that all the vendors will make losses corresponding in total to the sum withheld from spending; or, as will happen in practice, the total loss will be spread unevenly, and will fall most heavily on those vendors who are in the most vulnerable economic position. If the value of the total income available is A, and A is also the total cost of production of all the currently produced goods and services, and if B is withheld from spending on either capital goods or consumers' goods or services, it is clear that A − B cannot equal A, and that accordingly either some of the current output must be held back from sale—at a cost—or if the whole output is sold it must be sold for less than A.

When Keynes says that Savings necessarily and always equal Investment, he is drawing attention to the plain truth that money saved beyond what is invested is not really saved at all, from the social point of view: it is "spilt on the ground". I wish he had used some different phrase—'Social Savings', for example—to indicate this, and had continued to say, as he said earlier, that Savings (i.e. the sums which individuals or corporations *attempt to* save, and do succeed in saving from their own private standpoint) need not be equal to Investment. For it is this distinction between Savings (in the second sense) and Investment that is Keynes's chief improvement upon Hobson's essential thesis. Let us conclude that Savings, in the everyday sense of the word, need not equal Investment, whereas Social Savings must.

At this point the question is sometimes asked—But what happens to the money that is saved but not invested, so that, from the standpoint of the community, it is not really saved at all? The answer is that this money simply vanishes out of existence, or at all events out of active circulation. If all the business of exchanging goods and services were done with hard cash, it would presumably vanish into holes in the ground, safes, or bank vaults, or into whatever receptacles for idle money were in fashion in the community concerned. Where, as in modern societies, most money consists of book entries in bank ledgers, it is as easy to write down the total amount as to write it up. If there are smaller demands on the banks for credits, they simply stop replacing by fresh advances those which are repaid. The totals recorded in their ledgers fall off: the unused money disappears as easily as it came into being. In practice, the process is not quite so simple as these sentences suggest; but they give the gist, and there is no need here to enter into the details. To the extent to which this process of creating and annihilating money needs further explanation in connection with employment problems, the explanation will come better at a later stage.

There is a second point at which Keynes substantially alters the argument presented by Hobson. Hobson stresses the point that in good times a grossly uneven distribution of income leads to excessive Saving, which brings on a crisis. Keynes insists that in bad times there is much too little Investment, which involves severe unemployment among the producers of capital goods and indirectly through the loss of their purchasing power among the producers of consumers' goods and services as well. According to Hobson, there is too much Saving in good times: according to Keynes there is too little Investment in bad times. There is clearly nothing inconsistent in these two statements, though one stresses the too much and the other the too little. The difference of stress leads, however, to the stressing of different remedies. Hobson argues in favour of greater equality in the distribution of incomes and especially against wage-reductions at any time, because they will diminish the demand for consumers' goods and services. Keynes argues in favour of measures designed to maintain the level of Investment in bad times—or rather, in times which would be bad if the level of Investment were allowed to fall. Hobson puts the stress on the maintenance of consumers' demand: Keynes puts it on the maintenance of the demand for capital goods. How far are their views inconsistent or conflicting at this point?

The most obvious criticism of Hobson's statement of the causation of economic crises is that, whereas he attributes them mainly to a deficiency in the demand for consumers' goods and services, in fact the industries which suffer the most serious decline in bad times are those which produce not consumers' but capital goods. During the depressions between the wars the industry with the very worst record of unemployment was shipbuilding. Unemployment was also very severe in iron and steel manufacture and in the heavier branches of engineering. It was much less severe in light engineering, which includes a number of consumers' trades. The other cases of really bad unemployment in major industries were coal, cotton, and water and waterside transport. These are more complex cases. Coal is at once a consumers' good, a material used in all types of industry, but especially in iron and steel making and in transport, and an export. Cotton goods are produced much more for export than for the home market. The demand for the services of seamen and dockers depends mainly on the activity of import and export trade. Economic depressions usually affect exports more than production for the home market, because countries faced with a decline in activity and purchasing power usually try to reserve as much as possible of their home markets for their own producers. Thus, a consumers' good which is produced largely for export may experience as great a decline in demand as a capital good; but this does not invalidate the point that in general, as far as production for the home market is concerned, the industries producing capital goods are more adversely affected in times of depression than those producing consumers' goods and services. The depression in the coal industry was peculiarly bad because coal is both a material largely used by the capital goods industries and largely exported. The depression in cotton was aggravated by the fact that, though a consumers' good, it was manufactured mainly for export. The deep depression in shipping and the waterside industries was due to the general decline in overseas trade.

The tendency for investment and the production of capital goods to fall off in bad times more than the output of consumers' goods and services is perfectly easy to explain. The production of capital goods is made up of two broadly distinct groups—replacements and renewals of existing plant and the output of additional plant designed to expand the supply of instruments of production. The existing plant is always wearing out, or becoming obsolete, and needing to be replaced or renewed if the productive capacity of the economic system is to be maintained. It wears out, of course, at widely varying rates in different cases; but let us assume that the average annual need for replacements and renewals is 10 per cent of the existing equipment. Now suppose that total demand for all classes of goods and services falls from 100 in one year to 90 the next. The equipment which produced the output of 100 will, the next year, be capable of producing 90 without any renewals or replacements at all—or rather would be so, if it were all homogeneous, which of course it is not. It will, however, be possible, if total demand falls by 10 per cent, to postpone or do without a high proportion of the renewals and replacements which would have been made if demand had stayed at 100. There will accordingly be a very sharp fall—not 10 per cent, but more likely 50 per cent or more—in the demand for capital goods to replace those which are worn out or obsolete; and this fall will be the greater because, in view of the decline in demand and the consequent loss of profits, many firms will make do with obsolescent equipment which they would have replaced if times had been better.

The other part of the demand upon the capital goods industries consists of the demand for additional instruments of production over and above those needed to maintain productive power at its existing level. But why, if total demand is reduced, should there be any demand at all for *additional* instruments of production? It seems as if the fall in this part of the demand upon the capital goods industries would be catastrophic—from 100 in normal times to zero in bad times. In one sense, conditions will not be quite so disastrous as this; for even in bad times there will be some industries which will be expanding their productive capacity. If, however, we regard all investment in capital goods as belonging to renewals and replacements until enough has been expended in this way to maintain productive power at its previous level, it may well be that the *net* demand for *additional* instruments of production will be in bad times not merely zero, but a minus quantity. For the community as a whole may fail to maintain its aggregate productive power.

Some people find this argument confusing because they do not realise that, here again, the problem is being considered from the standpoint not of individual businesses but of the community as a whole. In many cases, when plant wears out or becomes obsolete, it is not replaced directly by its owners. Firms go out of business, and new firms come in; and there are shifts in the relative demand for different kinds of things, leading to decreases in the total equipment needed for making one thing, and increases in that needed for making another. From the standpoint of the community as a whole, the maintenance of productive capacity at its existing level means not that the productive capacity of each industry must remain unchanged, but that over all industries taken together must there be as much capacity as before to produce useful things, declines in some cases being balanced by increases in others. Thus, there is no *net* Investment in capital goods unless the total productive capacity of the community is raised above its previous level.

It is now quite plain why the industries producing capital goods are subject to wider fluctuations in the demand for their products than the industries producing consumers' goods for the home market. Any decline in the demand for consumers' goods will directly cause a greater decline in the capital goods industries. There is only one qualification that needs to be made. The demand for capital goods is governed, owing to the time factor, rather by the *expected* than by the *actual* state of consumers' demand. In the early stages of a depression, things are generally expected to get worse, and this aggravates the fall in the demand for capital goods. But the situation is changed at the first sign of recovery, or when conditions are expected to get better; for then not only is the demand for capital goods governed by the expected higher level of consumers' demand, but in addition the prices of capital goods are expected to rise, so that there is an advantage in buying them quickly before the advance in prices has occurred, or gone far. Accordingly, the early stages of a recovery that is expected to continue are marked by a brisk demand for capital goods, both to make up arrears of replacements and renewals and to expand total capacity to new levels.

Thus, *whether or not* a decline in investment is the main *cause* of trade depressions, it is an undoubted fact that depressions do involve a more serious decline in the industries producing capital goods than elsewhere. Keynes fastens on this fact, and argues that the best way of preventing trade depressions is to hold the volume of investment steady at the level needed to maintain a condition of full employment. In effect he is saying that, if employment in the capital goods industries is kept at the right level, employment in the fields of consumers' goods and services will, for the most part, look after itself, or at any rate the problem of maintaining it at an adequate level will become very much easier to solve.

This raises the question—Is there a right level for employment in the industries producing capital goods, and, if so, on what does that level depend? The answer of the orthodox, *laissez-faire* economists is that the right level is any level which the possessors of incomes themselves choose by deciding to save certain proportions of their incomes instead of spending them on immediate consumption. There is, however, as we have seen no necessary correspondence between the sums which private persons decide to save and the sums which other persons, or the same persons in some cases, decide to apply to the purchase of additional instruments of production. The volume of attempted private saving does not in any way determine the volume of investment. Less than persons attempt to save may be invested if some savings are not transferred to productive use; and more money than is saved may be invested if the promoters of new enterprise secure additional resources out of new money created by the banks. It is therefore a fallacy to suppose that the possessors of incomes, in deciding what proportion of them to withhold from expenditure on current consumption, automatically settle the scale on which investment in capital goods is to take place. Such investment, so far from being stimulated by saving in itself, is discouraged by it; for a mere decision to abstain from buying consumers' goods or services renders the production of them less attractive, to those who are in search of profits.

No doubt, the volume of *voluntary* savings does set a limit to the amount that can be invested, unless the banks provide additional resources for investment out of money which they create. If the supply of money were fixed, or were restricted to the total represented by the current incomes arising out of production, voluntary saving would, in a *laissez-faire* economy, set an upper limit beyond which investment could not go. It would not, however, set any lower limit; for there would be nothing to ensure that the whole of the money withheld from current consumption would in fact be spent on capital goods.

I have stressed the word *voluntary* in the preceding paragraph, because it is always possible for the State, or the local governing authorities, to raise money by taxation falling on incomes and to spend this money on the purchase of capital goods. Such taxation may have some effect in reducing the amounts which are voluntarily saved by the possessors of incomes; but they are most unlikely to cause voluntary savings to fall by the whole amount of the taxes in question. Their effect is therefore to cause a larger proportion of the national income to be saved (and invested) than would be the case if the taxes were not imposed. They impose upon the community some amount of *forced*, as distinct from voluntary, saving.

Banks, in creating additional money for expenditure on capital goods, are sometimes said similarly to inflict 'forced saving' on the possessors of incomes. If out of a supply of money, $x + y$, the recipients voluntarily save y, and the banks then create a further supply, z, which is all saved and invested, the proportion of the national income saved is bound to be greater than it would otherwise be. x is a smaller proportion of $x + y + z$ than it is of $x + y$. To be sure, the possessors of incomes can react by saving less than before; but they are unlikely to react to such an extent as to make $y_2 + z$ less than y was before z was brought into being. If, however, the result of creating z is to add to the current supply of goods and services in at least the same proportion as z adds to the supply of money, the recipients of incomes may be able, without reducing their savings, to buy at least as many consumers' goods and services as before. In such a case, their so-called 'forced saving' is without any physical cost or sacrifice on their part. A sacrifice is involved only if the effect of the new bank money is to raise the prices of goods and services, and so reduce the real value of their incomes. This is a question which we need not discuss further now, as it has been dealt with earlier in this book.

If the level of voluntary savings does not, as the orthodox economists appeared to suppose, determine the level of investment, what does? Clearly, as far as private investment is concerned, the determinant is the expectation of profit. Persons will invest their own money if the advantages of doing so, in terms of expected profit, seem likely to outweigh the advantages of not investing it; and persons will borrow money, from other possessors of money resources or from the banks, if they see a good prospect of a profit in excess of the interest which they will have to pay on the borrowed money.

The level of private investment is therefore determined by the expectations which persons of enterprise entertain of the prospects of profit, and by the relation which these expectations bear to current rates of interest. Keynes, by the way, very obscurely calls this psychological expectation of profit the 'marginal efficiency of capital'; but that is only one of many terms which economists have invented, apparently for the purpose of making Economics harder for ordinary people to understand. This expectation of profit, being a state of many people's minds, is necessarily a somewhat nebulous conception. The prospective profit that enters into consideration is not merely that of the next month or year or even decade. The period taken into account will differ for different kinds of investment, according to the period of time over which the capital will be locked up, or, in other words, the expected 'life' of the capital goods to be bought with the money. It will be longer for buildings than for machinery, and usually longer for heavy than for light machines. It will also be affected by the propensity of men to pay less regard to distant than to near prospects—a propensity which varies not only from one person to another, but also from periods of relative stability to periods in which no one ventures to prophesy for long ahead. Moreover, the estimates which men make of their prospects of profit will differ very widely according to the state of mind they are in; and this will be affected for most of them by all sorts of factors which go to the making of mass-psychology. There is accordingly no saying that such and such a prospect of profit will produce such and such a level of willingness to invest. It will all depend on the mood men are in; and it will also, as we shall see later, depend very greatly on the nature of the business structure within which they have to act. A business structure largely dominated by monopoly will not 'behave' in the same way as one in which free competition is mainly prevalent.

This intangible psychological force does not, however, by itself determine the volume of investment. It interacts with another factor—the level of interest rates. We are therefore faced by a further question. What determines interest rates for the various kinds of loan? The older economists, thinking in terms of one 'rate of interest' *par excellence*, to which all the varying rates actually paid were somehow related, argued that the rate of interest was the outcome of the higgling of the market between borrowers and lenders. The higher the rate of interest, the more money would people be willing to save, and the less would they be willing to borrow; and accordingly the rate would settle at the level that would just equate the supply and the demand. It can be agreed that, *other things being equal*, high interest rates will deter borrowers; for clearly there will be projects which will offer a sufficiently attractive prospect of profit if interest is at x per cent, but not if the rate rises to $x + 1$. It is, however, doubtful whether, save at very high levels of interest, this is a factor of much importance outside a fairly narrow range of industries in which interest charges form a high proportion of total cost. The industries in which this is the case include building, which is, as we shall see, of crucial importance in relation to investment policy;[1] but in most manufacturing industries and services interest rates do not appear in practice to have a big influence on the decisions of business men for or against buying capital goods or expanding production. This is partly because nowadays businesses finance expansion so largely out of their own accumulated reserves of profits, on which, of course, they do not have to pay interest, though they do have to forego the interest they would receive if they lent these reserves out to others instead of using them themselves. It is also partly because bank interest and other forms of short-term interest usually form only a very small element in total costs.

The exceptional cases in which long-term interest rates are of significant influence on the volume of borrowing for investment are, however, important enough to be taken seriously. They in-

[1] See pages 87 and 163.

clude, besides building, such major enterprises as railways, power-stations, docks, ships, and other large-scale services.[1] But it must not be supposed that, even in these industries, it is the absolute level of interest rates that determines the willingness to borrow for investment. Always, it is the level of interest in relation to the expectation of profit. Actually, more has usually been borrowed when interest rates have been fairly high, because the expectations of profit have also been high at such times.

What has been said leads to the conclusion that, even if there are many borrowers who are not greatly affected in their investment activities by the rates of interest they are called upon to pay, there are probably enough borrowers who are affected to exercise a considerable influence *at the margin*, where the rates are determined. This applies at all events to long-term rates, though it probably applies but little under most conditions to the rates of short-term borrowing. But what of the other blade of the classical pair of scissors? Is it true that the higher the rates of interest, the larger will be the volume of money offered for lending? This is a highly complicated question. There are many savers who will in practice tend to keep their savings steady irrespective of interest rates; and there are others who will positively save more as interest rates fall. The steady savers include those who are saving under contractual arrangements fixed over a period of years—buying their houses on the instalment plan, paying regular fixed premiums on insurance policies, purchasing annuities, and the like. The savers who save more as interest rates fall are those who are seeking to accumulate a capital sum sufficient to yield a certain money income; for the lower the rate of interest the larger any such sum will need to be. To the opposite camp belong those who save 'for profit', and will save more if the offered return is greater. But these are certainly much less numerous than the steady savers, and probably account for much less saving than those who behave in the opposite way. Finally, there are those who save out of big incomes what they do not want to spend, and there are the business concerns and corporations which build up reserves with a view to the future. Of these, the former are almost entirely uninfluenced by interest rates, save in the sense that if their current incomes are reduced by low interest rates they will have a smaller surplus over what they want to spend, and will therefore save less; while the latter will tend to accumulate large reserves when profits are high, and to accumulate much less or even to dissipate part of their reserves in dividends in bad times, but will be very little influenced in this respect by interest rates of any kind.

The forces on the supply side which influence interest rates are

[1] See page 163.

therefore many and conflicting, and it is certainly not legitimate to assert that in the aggregate higher interest rates will elicit an increased volume of saving. Indeed, the effect may be just the opposite, and no general statement can be made. It is therefore quite out of the question to accept the orthodox notion that interest rates are determined by the interaction of supply and demand forces, in such a way that lower rates mean less saving and more borrowing, and *vice versa.* This would not be true even if there were not—as there is—the possibility of additional supplies of money for lending being created by the banks. In view of this possibility, it becomes mere nonsense to speak of interest rates as being determined by the relation at the margin between readiness to save and readiness to borrow. For the 'marginal saver' is in effect not the person who is induced to save or not to save by the rate of interest which his money will command, but the banker, who can create more or less money, and thus determine the rates at which borrowing can take place.

What this means is that interest rates are not, as the orthodox economists used to suppose, the result on the supply side of the greater or less willingness of the owners of income to forego current consumption in the hope of prospective gain. They depend on monetary policy, on banking law and practice, on deliberate decisions taken by financial authorities or, even in the absence of such deliberate decisions, on what the financial authorities actually do. Any rate of interest is, of course, a potential deterrent to borrowers, who, in any given economic situation, will in the aggregate be ready to borrow more as the rates of interest fall. But the point at which the demand for borrowed money is cut off by this deterrent is fixed, not by any process of interaction, but by the banks. The policy of 'cheap money', as a means of inducing a high level of investment, is based upon a recognition of this fact.

But, of course, the rates of interest alone do not, any more than the expectations of the business men about the future state of demand, settle how much investment there will be on private account. It is the interaction of these two forces that determines the level of investment. Banks may lower interest rates to any extent, and achieve no increase in the volume of investment, if business men are feeling so pessimistic about the future that no fall in the rates will induce them to extend their borrowing. The banks can always set limits to the expansion of investment; for if high interest rates are ineffective in deterring enough borrowers they can always refuse to lend, by raising the standards of creditworthiness on which they insist from those who ask for loans. But banks cannot with the same certainty expand the volume of investment; for though they may offer 'cheap money', they cannot force anyone to borrow from them unless he sees a prospect of profit as a result. If a business man thinks he is more likely to make an actual loss than a profit, clearly even a zero rate of interest will not induce him to borrow. A *negative* rate, i.e. an actual payment for the favour of taking the money, no doubt might, if it were big enough; and this is in effect what is done when subsidies are offered by the State in order to induce 'shy' business men to undertake investments which are not attractive on their own merits. Banks, however, at any rate when they are private institutions, do not offer subsidies. There are limits, set by their own costs, below which they will not reduce their rates; and, if these *minima* are higher than most potential borrowers are ready to pay, the loans are not made, and the policy of creating additional bank money cannot be effectively pursued.

The upshot of the argument so far presented in this chapter is that (*a*) the industries producing capital goods are on the whole liable to larger fluctuations than the industries producing consumers' goods and services; (*b*) if the rate of investment in capital goods can be held steady, the effect will be to maintain activity in the consumers' goods industries as well; (*c*) the rate of investment is determined by the interaction of the profit expectations of business men and the rates of interest at which money can be borrowed; (*d*) the rates of interest are of much greater influence in some industries than in others, and are notably influential in building and other constructional industries which use a high proportion of long-term capital; (*e*) the rates of interest are mainly determined, not by the greater or less 'abstinence' or willingness to save of the owners of incomes, but by bank policy; (*f*) bank policy is much more certainly effective in restricting investment than in expanding it; (*g*) the principal factor leading to expansion, or the lack of it, is the degree of confidence felt by business men in the prospects of profit-making.

If these conclusions are accepted, we can go back to our question—Is there a *right* level of investment for a community at any given time? The answer clearly is that there is not, in any sense in which 'rightness' implies something about which all reasonable persons can be expected to agree. If the level of investment were determined by the willingness of the owners of incomes to postpone consumption, it could be argued that the actual rate of accumulation of capital reached in this way had a certain psychological 'rightness', as corresponding to men's actual wills. But it is not so determined, and accordingly this contention is ruled out. What is left is the notion that the level of investment can be influenced by banking policy, interacting with the degree of confidence in the future felt by business men. There is, however, plainly no assurance that the resultant of these forces will embody any objective rightness.

We have, then, in looking for a criterion of 'rightness', to discard what actually happens under the existing conditions, and to pursue our inquiry along a different line. What proportion of its annual income ought a community to save and invest, in the sense of applying a part of its output to the satisfaction of future rather than present needs? There is evidently no simple answer to this question; but there are a number of relevant considerations which ought to be taken into account. If population is expected to increase, or if, in a stationary or declining population, the proportion of persons needing to be supported by those who work is expected to increase, that constitutes an argument for a higher rate of saving and investment than would be called for in a community stationary in population and in age and sex structure. If the community is 'backward' economically, that is, if it is by modern standards under-equipped with instruments of production, that again constitutes an argument for a high rate of accumulation, even at the cost of considerable privation while the capital structure is being raised to a higher potential. Of course, this sort of privation may not be necessary if the requisite capital goods can be obtained on loan from richer countries on terms not too onerous to the borrowers. On the other hand, a community which is well-equipped with capital goods as a result of past accumulation may quite reasonably decide to reduce its rate of saving and investment; for what is investment for except to provide for increased future consumption; and where is the point of it if this increased consumption is to be for ever postponed?

It is often said that, in addition to such considerations as these, the desirable rate of investment will vary with the current pace of technical change. Clearly, a community will need to spend more on capital goods if its existing stock of such goods is becoming more rapidly obsolete as a consequence of new inventions or of changes in demand. It is, however, a matter of terminology whether we choose to regard new instruments of production acquired as a result of technical change to replace old ones as constituting 'Investment', or as replacements and renewals of the existing plant. In either case, the greater the pace of technical change (and also of changes on the demand side) the larger will the industries producing capital goods need to be. The rate of 'Gross Investment' (including replacements and renewals) will need to be greater: the rate of 'Net Investment' (excluding replacements and renewals in the widest sense) will be unaffected.

Finally, we come to the conclusion that the rate of investment—

of net investment, that is, which a community adopts is a matter of choice. There may be good reasons for choosing a higher or a lower rate, according to circumstances; but there is no objectively determinable 'right' rate. The decision is a matter for statesmanship and commonsense, taking all the relevant factors into account. People are bound to differ about it, and no one can *prove* exactly what the rate ought to be. It is, however, fairly evident that at the end of a war which has both wasted considerable capital assets and required much postponement of normal capital construction, and has also so upset conditions as to make certain large changes both in the conditions of demand and in the technique of supply, a high rate of capital accumulation is likely to be desirable until arrears have been overtaken and adaptation to the new conditions has been achieved. This adds force to the view that, whatever may have been the 'right' level for investment in 1939, the level is likely to be a good deal higher when peace returns. It therefore appears that theories which stress the need for the maintenance of a high level of investment possess, for the present generation, a pragmatical rightness.

CHAPTER IV

WAGES AND EMPLOYMENT

DOES IT, however, follow that, because the level of investment after the war ought to be relatively high, the rate of consumption ought to be correspondingly low? On one assumption, it does follow. If the community is *in any case* going to make full use of all its productive resources in making things either for investment or for immediate consumption, it follows that the more things it makes for investment the fewer it will be able to spare for the consumers' immediate use. In this sense, it is true that we cannot both eat our cake and have it; but it is essential to understand that this holds good only on the assumption that 'full employment' exists. It is very far from being true that in the past less investment has meant more consumption, or more consumption less investment. The two have usually been relatively high or low at the same periods; and unemployment has been small when they have been high, and widespread when they have been low.

It is a very curious fact that most economists have gone on for so long basing their doctrines on the assumption that there are jobs for all, even when they have been fully conscious of the existence of unemployment as a social problem. They have reconciled their theories with their awareness of the facts by assuming that unemployment is the result, partly of a mysterious force which they have called the 'trade cycle', and partly of the wickedness or folly of various classes of persons in standing out against the working of economic laws. In particular, they have very often denounced Trade Unionism as a great cause of unemployment, on the double ground that the Unions, by standing out for unduly high wages, have restricted the ability of employers to employ labour at a profit, and that Trade Union rules about apprenticeship, the 'right to a craft', and so on, have unduly limited the mobility of labour. Latterly, they have also complained that Social Insurance limits mobility, and makes it easier for unemployed workmen to refuse inferior jobs which they ought to take. All these complaints are commonly summed up in the phrase that there are undue 'rigidities' in the supply of labour.

This body of doctrine runs, of course, directly counter to Hobson's insistence on the need to maintain consumption in order to avoid trade depressions. Hobson argued that wages ought to be maintained in periods of depression, in order to sustain the demand for consumers' goods and services, and thus indirectly sustain the demand for capital goods as well—for the greater the demand for consumers' goods the greater would be the demand for capital goods to be employed in producing them. The orthodox answer to this argument was in the first place the apparently simple statement, as of a self-evident fact, that the cheaper labour was the more of it employers would be prepared to use, and in the second place the contention that, if the workers would but accept lower wages and thus get back to work, prices would fall and the lower money wages would soon buy as many commodities as the higher wages had bought before. It was not realised that these two contentions were really inconsistent; yet there is clearly no reason why employers should go on employing additional labour if, by an all-round fall in prices, the relation of wages and prices has again become the same as it was when, *ex hypothesi*, unemployment did exist on a considerable scale. The orthodox economists tried to have it both ways, because they set out from an initial assumption that there was a natural tendency in the economic world towards 'full employment'. If unemployment was nevertheless found to be prevalent, it must be due to some abnormal factor. Remove this factor, and all would be well.

In truth, however, the apparently simple statement about the relation between wages and employment rests on one of the most elementary of logical fallacies—the fallacy of composition. It is quite true that any particular employer will have an inducement to use more labour the cheaper labour is, either because cheaper labour lowers his costs and so enables him to sell more of his products at lower prices or because the cheaper labour induces him to substitute labour for other factors of production. This, however, holds good only on the assumption that everything else remains the same, including the wages paid by other employers, or at all events by employers in other industries. As long as the purchasing power of other people remains as it was, a fall in the purchasing power of his own employees will not have any appreciable effect on the conditions of demand for his products; and as long as the fall is confined to a single industry the effect on demand will not be great, unless the industry employs a considerable fraction of the entire working population. As soon, however, as the fall in wages is generalised, the conditions of demand for the products of all industries are affected, and it is no longer possible to argue that a fall in wages will *necessarily* be followed by an increase in the numbers employed. It may be, or it may not: whether it will or will not must depend on the particular circumstances of the case.

We have seen that, if *all* prices were to fall in the same proportion as wages, the resulting level of employment could be expected to be neither greater nor less than before; for an *all-round* change in prices would leave the essential forces quite unchanged. But an all-round reduction in wages only would clearly not cause *all* prices to fall in the same proportion as wages, because it would not involve a reduction in all costs. Only wage-costs would be directly affected; and wage-costs bear very different relations to total costs in different branches of production. Thus, even if prices were at once reduced in proportion to the fall in costs, they would be reduced by different percentages for different products, and the average reduction would be a great deal less than the average reduction in wages.[1] Demand therefore would not expand but contract, as far as the wage-earners are concerned; and it seems likely that the fall in wages would reduce employment rather than cause it to increase. It is true that the non-wage-earners who had not suffered a cut in income would be able to buy more in proportion to the fall in prices; but they would be most unlikely to spend the whole of their increased real incomes on consumers' goods and services, and if they tried to save more there would be no good reason to expect a rise in investment in capital goods, since there would be no expansion in consumers' demand to make such investment profitable.

[1] Moreover, some industries are much more subject than others to monopoly control; and accordingly the reactions of changing costs on prices would differ from one industry to another.

Is there, then, no basis, except an obvious logical fallacy, for the deeply rooted belief that wage-reductions are calculated to cause an expansion of employment? There is such a basis, though it is by no means broad enough to bear the conclusions which are often rested upon it. In the first place, a reduction in wages can induce employers to use, in making any given supply of goods, more labour and less of other factors of production whose prices have not been reduced. This will react on the demands made on the capital goods industries; but the reaction may be slow. It will react to some extent on the prices offered for the use of the other factors, and help to bring them down in sympathy with the movement of wages. But, as we have seen, the logical end of this process will be to leave the economy with precisely the same amount of unemployment as it started with; for as soon as the other factors have become as cheap as labour, the reason for substituting labour for them will disappear. Nothing much can be rested on this shaky foundation, even in the short run: in the long run, nothing at all.

In the second place, wage-reductions, by lowering costs, may make it possible to sell more goods abroad. This is the real foundation for the belief in lower wages as a means of increasing employment. If wages fall in one country *and not in others*, the country affected will be able to offer its exports at lower prices and therefore to sell more of them, as the purchasing power of the foreign buyers will remain as high as before. Accordingly, lower wages may lead to more employment if they cause an expansion of exports exceeding the fall in home demand. But, of course, this advantage will soon be lost if other countries either follow suit and reduce wages to a like extent, or set up protective barriers in the way of the admission of goods from the wage-reducing country.

In practice, what happened between the wars was that the pressure for wage-reductions came chiefly from the exporting industries or from industries which were subject to competition from imports made abroad by cheap labour or aided by currency depreciation. In these particular industries, it was sometimes quite possible for wage-reductions to lead to an expansion of employment, at any rate in the short run. The deduction from these cases was generalised, and was used to reinforce the fallacious arguments of the theoretical economists.

The reason why, apart from this special case, wage-reductions are unlikely to cause an expansion of employment is, of course, that wages occupy a dual position in the economic system, as both costs and incomes. If they are regarded one-sidedly as costs, it seems commonsense to expect a fall in them to expand employment: if they are regarded one-sidedly as incomes, exactly the opposite conclusion seems to emerge. As they are in essence both, no *a priori* conclusion can legitimately be drawn.

It is, however, a very pertinent fact that wages, as a form of income, account in industrial countries for a very large proportion of total consumers' demand, and that of the incomes paid out in wages a very high proportion is normally spent at once on consumers' goods and services. No doubt, working-class savings amount, in the aggregate, to a very considerable sum; but this sum is much smaller, as a proportion of working-class income, than savings are of the incomes of the richer classes, at all events in normal times.[1] Moreover, the largest volume of savings in the modern world is institutional; and a large part of this saving is made not out of personal incomes but out of the reserved profits of companies which are never distributed to individual owners as incomes. Accordingly, a fall in wages hits just that part of the national spending which is most directed to the purchase of consumers' goods and services. It is calculated, apart from the special case of exports, to react strongly on the demand for such things, and to bring about a contraction of employment in the industries supplying them.

It seems, then, as if Hobson was right in arguing that wages ought to be maintained, and not reduced, during a slump. Keynes reaches the same conclusion, but by a quite different route. He lays stress on the distinction between 'money wages' and 'real wages'—that is, what the money wages will buy—and argues that often reductions in money wages are not reductions in real wages, because prices fall faster than wages are reduced. I do not of course deny that this can happen, or that it has happened to some extent in more than one slump. But I do deny that a fall in money wages can of itself cause a proportionate or more than proportionate all-round fall in prices. There may be, and sometimes are, other forces at work which bring down prices faster than money wages can be reduced; but that is not the same thing. For example, in Great Britain in the great slump of the nineteen-thirties the cost of living fell on the whole faster than wage-rates, mainly as a result of the catastrophic fall in the price of agricultural imports. But this does not go to prove that real wages would have risen more if money wages had been cut still further. Moreover, the calculations which Keynes makes on this point are mainly in terms of wage-rates, which are not the same thing as earnings. Real earnings may fall in a depression, as a result of short time and the cessation of overtime and high piece-

[1] War upsets this, as well as many other normal conditions of capitalist enterprise. But I am not talking now of what happens in time of war.

work earnings, even when real wage-rates have increased or remained unchanged.

The gist of Keynes's argument at this point is that workmen and Trade Unions are much 'stickier' in terms of money wages than of real wages. They will refuse to accept a cut in money wages, even if prices are likely to fall enough to leave their real wages intact; but they will show much less zeal in insisting on higher money wages when prices rise. There is something in this; but not, I think, a great deal. It is true that the workers do all they can to resist reductions in money wages; but it is not true that the acceptance of such reductions would cause prices to fall to an equal, or perhaps to a greater, extent. The workers are quite right in resisting reductions in money wages to the best of their power. If prices would fall by as much as the money wages were reduced, by how much less would they fall if money wages remained unchanged? The worker's aim is to improve his economic position, not merely to keep it intact. His right course is to press all the time for the highest level of money wages he can get.[1]

This doctrine has, however, to be qualified before it can be applied to the particular, as well as the general, case. The higher wages in general are, the better, up to the point required for achieving full employment. But it is of course true that the workmen in any particular trade can by pressing for higher wages divert employment from that trade to others. If they attempt to behave as sectional monopolists of a particular kind of labour power, they may, like other monopolists, better their own position, but only at the cost of lowering the demand for the commodity they produce. In order to pursue such a policy, they will have either to limit successfully the numbers in the trade concerned, or to carry a burden of unemployment. Higher wages are good for employment and production only to the extent to which they are widely diffused. Sectional monopolies, in labour as much as in anything else, restrict employment and production in the industries to which they apply. How far they also restrict total production in all industries it is not so easy to say. If the workmen-monopolists spend their additional incomes on consumers' goods and services, the effect is to divert employment from their own trade to others whose products they buy. If they save these incomes, the effect is to restrict employment. Or rather, these are the direct effects; but in practice there are usually indirect effects as well. Labour monopoly commonly coexists with monopoly on the employers' side. It is thus instrumental in forcing up prices and restricting output beyond what is involved in the higher wage. As soon as it takes this form, it becomes

[1] Again, of course, I am not speaking of what applies in time of war.

restrictive of production and employment generally, and not merely in the trade concerned. All private monopolies are anti-social: the most dangerous form of them is that in which capitalists and workers become in effect partners in exploiting the public.

CHAPTER V

STRUCTURAL AND CYCLICAL UNEMPLOYMENT

WHAT CONCLUSIONS can be drawn from the foregoing chapters about the conditions which are necessary in order to establish, and to maintain, a state of 'full employment'? It must be borne in mind that we have been discussing, so far, exclusively what happens in a society in which most of the instruments of production are privately owned and the provision of employment is mainly a matter of the willingness of the private directors of these instruments to engage labour. We have been speaking, moreover, of a kind of society in which the accumulation of new capital is done mainly by private persons or firms, with capital supplied either out of their own savings, including business reserves, or by raising money in the private capital markets or securing loans from banks or other financial agencies.

We have seen that in such a society it is by no means a foregone conclusion that the resources of production will be fully employed, or even that there will be any underlying tendency towards full employment. It is simply not true that there is in such a society a tendency to move towards a position of 'equilibrium' in which all usable resources will be put to use. There may be, as Keynes says, no level of wages at which all labour will be able to find employment: there may be no way in which the economy can move out of a condition of stagnation under the sole impulsion of the profit motive. It is not worth arguing whether this would still be true if society were in fact like the ideal capitalist societies about which economists so often prefer to write; for there are no societies which sufficiently resemble these ideal societies for anything useful to be learnt by studying their imaginary behaviour. The societies we have to deal with if we are out to abolish unemployment are the real societies in which unemployment exists, not merely because there is a screw loose somewhere, so that the mechanism is not working properly, but as a standing feature, worse at some times than at others, but continually present and liable to the recurrent superposition of super-unemployment.

In these societies, unemployment, as a social disease, takes two main forms—cyclical and structural—over and above the familiar forms of casual, seasonal and frictional unemployment. It is worth while to make war on these latter forms of unemployment wherever we can—to decasualise dock labour and other kinds of labour peculiarly subject to casual conditions; to do what can be done to even out seasonal fluctuations in demand and in production, or sometimes to dovetail seasonal trades which have different peak periods; and to lessen the frictional unemployment involved in changing jobs by providing a thoroughly efficient service of Employment Exchanges, and also by making easier the migration of labour from place to place or from trade to trade. But even if we were successful by these measures in cutting down casual, seasonal and frictional unemployment to a very great extent, we should still not have reached the core of the unemployment problem. If, by decasualisation, we cause fewer people to compete for work at the docks, the result is that there are more left to seek employment elsewhere. Similarly, if we dovetail seasonal trades or reduce the waste of working time between job and job, fewer workers will be able to do as much work as a larger number did previously; and unless there are additional jobs to absorb the surplus, there will be more people out of work than there were before, though there will be less under-employment.

In saying this, I do not want to run the risk of being supposed to argue that there is a 'work-fund', as some of the older economists used to believe that there was a 'wages fund', imposing impassable limits on the amount of employment that a community can provide for its members. I do not, for example, hold that an increase in population carries with it the prospect of an increase in unemployment—not even if the addition to the population consists mainly of immigrants of working age. It is, no doubt, fully possible under certain circumstances that a rise in population may increase unemployment, or a decrease in population cause it to decrease; but there is no certainty that this will happen, and the effects may well be of an opposite kind. Immigration, for instance, is usually in the main of persons in the prime of life; and, even if they bring no purchasing power with them from abroad, they will have to be fed and their arrival will probably have some stimulating effect on consumers' demand and thus cause some expansion in employment, though not necessarily enough to absorb them all in jobs. On the other hand, emigration tends as a rule to remove persons whose productive power is above the general average, and thus to lower the marginal efficiency of the remaining labour, and to depress employment, though not necessarily so much as to offset the entire body of emigrants. If we rule out migration and consider only population changes due to changes in birth or death rates, we have to reckon with the fact that a rising birth-rate, by increasing the number of children, lowers temporarily the proportion of occupied to total population; whereas a falling death-rate produces a similar effect by increasing the proportion of retired persons. Such conditions exert a pressure in the direction of increased consumption and therefore tend to raise the level of employment. On the other hand, a falling birth-rate decreases the proportion of children and increases the proportion of occupied to total population. Where such a state of affairs is not offset by a falling death-rate, the rate of consumption will tend on the whole to fall.

In effect, the relations between population movements and employment are highly complex; and any attempt to discuss them here would lead us much too far afield. All we need note is that a rise in the birth-rate first decreases and later increases the proportion of occupied to total population, whereas a fall increases this proportion. A fall in the death-rate, if it affects mainly infant mortality, has the same effects as a rise in the birth-rate: if it is the result of a prolongation of adult life, it is likely to decrease the proportion of occupied persons, by adding to the number of old people retired from work.

The two forms of unemployment which offer the fundamental challenge are cyclical and structural unemployment. Of these, cyclical unemployment arises when, over industry as a whole, the combined demand for capital goods and consumers' goods and services falls off, as it does in periods of general trade depression. Structural unemployment, on the other hand, though it gets worse when trade generally is bad, is not a product of the 'trade cycle'. It arises when, for any reason, the productive structure of the community has got out of adjustment to the structure of demand, so that there are *specialised* resources of production—skilled labour and specialised machinery, for example—which are not adapted to making the things people want more of, or at any rate the things of which people are prepared to pay for larger supplies. Such structural maladjustments can arise either out of changes in what people want, or out of changes in the technique of production, or, again, out of changes in the conditions of overseas trade. They are most serious where they affect industries in which large bodies of skilled workers have been engaged, or large masses of expensive capital goods have been locked up—or, of course, both.

Let us consider first this problem of structural unemployment. Changes in consumers' wants may on occasion put a whole industry out of business; but much more often what occurs is a gradual decline. Lace curtains and horse-drawn carriage building furnish cases in point. Tastes changed; and the demand for these things steadily fell off, leaving the skilled workers previously employed in making them the prey of unemployment unless they could adapt themselves to new jobs, and driving into bankruptcy or winding-up many businesses which were not able to turn over to new lines of output. Decline in demand for a product can arise from a variety of causes. A thing may quite simply go out of fashion, as lace curtains have done; it may be superseded by a new trade, as horse-drawn carriage building has been by motor-body building. Or a thing may come to be less in demand because the types of persons who used to buy it have fallen off in numbers or have had their incomes reduced—as would occur in the case of many high-quality luxury products if incomes came to be less unequally distributed.

It is not easy to keep such changes originating on the demand side distinct from changes which are due to altered technical conditions. The decline in the demand for horse-drawn vehicles was mainly due to the development of the motor-car, and can be regarded as due to conditions changing on the supply side rather than to a decline in the taste for broughams and hansom-cabs. Similarly, if artificial silk stockings and other garments come into use in place of garments made of wool, or cotton, or linen, or real silk, the community is faced with a change in demand which is the outcome of changed technical conditions of supply. Most demand changes, except those which are due to a change in the distribution of incomes or in the total wealth of a society, are of this kind, and are traceable to changes in the technique of production rather than to independent changes of valuation in the consumers' minds. But no hard and fast line can or should be drawn. The modern preference in certain social strata for living in smaller houses or flats and spending less on service in the home, so as to have more to spend on amusement outside the home, is partly due to the allurement of better cinemas, restaurants, dance-halls, road-houses and the like, and to the development of road services, and partly to a change in social attitudes which is inextricably mixed up with these technical changes, but cannot be regarded as simply one of their effects.

It is easy to see that, the greater the pace of technical change, the greater is the risk of structural maladjustments in the economic system. Naturally, the consequences are least serious where the superseded branches of production employed neither large numbers of highly skilled workers nor large quantities of expensive and highly specialised plant. The less specialised worker can be transferred more easily than the worker whose main asset is a highly specific kind of skill: light machinery, built to last for only a short time, can be written off much more easily than expensive machinery designed to yield up its value over a long period of years. When the pace of technical change is expected to be rapid, there is a tendency, wherever possible, to build less durable, and less costly, plant, in order to reduce the risks of obsolescence or failure of demand.

Structural unemployment, we have seen, may arise not only from a decline in home demand due to changes in consumers' wants or to technical changes in the means of meeting them, but also from changes in the conditions of overseas trade. The calamities of the British cotton industry have been due very much less to the substitution of rayon for cotton than to the fall in exports, which in turn has been due, not to a decline in world demand, but to the rise of production in the Far East and in other areas which used to be Lancashire's principal customers. When such declines in exports occur, the problem of structural unemployment is apt to appear in its most intractable form, because those who suffer under it are much less ready to believe in its permanence and inevitability when their trade has been lost to others than when it has ceased to exist, and they are accordingly apt to be much slower in tackling the unavoidable problems of readjustment. Many people in Lancashire went on hoping against hope for a return of the good old times, long after all prospect of such a return had disappeared. Consequently, they refused to cut their losses, and, by nursing false hopes, rendered their position a good deal worse than it need have been.

The industries in Great Britain that were principally affected by structural unemployment between the wars were coal, cotton and shipbuilding. Of these, the coal industry was a very large employer of very highly specialised labour, accustomed to relatively high wages, and very difficult to transfer to other uses—the more so because migration to a new area as well as to a new trade was usually involved. The cotton industry also employed a number of highly specialised bodies of craftsmen—spinners, weavers, bleachers, dyers and so on—who were very difficult to move to alternative jobs; and the industry was also one in which very long-lasting machinery was used, so that the amount of fixed capital locked up in it was high—though this factor was modified by the high average age of the machines, especially on the manufacturing side. Shipbuilding was also an industry using both expensive and highly specialised plant and a high proportion of very skilled, specialised labour not easily transferable to any other trade.

Consequently, the problems presented by structural maladjustment in Great Britain between the wars were exceptionally difficult to deal with. In coal and cotton they were, for a long time, hardly dealt with at all; and when an attempt was made to put the coal industry in some sort of order this was done by turning the coal-owners into a legally sanctioned monopoly privileged to exploit the public rather than by reorganising the industry to fit the changed conditions. Very tentative provisions for reorganisation were made in the successive Acts passed between 1930 and the outbreak of war; but they were so hesitantly made, and so left without effective sanction, that the coal-owners' vigorous opposition easily brought them to nothing. In the case of shipbuilding, on the other hand, the problem was tackled, by a private monopoly created by the leading firms with the aid of the Bank of England, so effectively that the outbreak of war found this country with its shipbuilding capacity about halved, and the discarded sites sold under conditions which in many cases made it impracticable to bring them back into use. It may seem ungracious to grumble at the cotton industry for doing too little and at the shipbuilding industry for doing too much. But that is what happened. The shipbuilders, having erected themselves into a monopoly, proceeded to play the monopolists' game by not merely eliminating productive capacity that was really redundant in relation to the potential demand, but going beyond this and scaling down capacity to the level at which it offered the most attractive prospect of monopoly profit. In this they acted without any regard for the fortunes of the skilled workers, who were left to rot away jobless in the deserted shipyard towns.

Structural unemployment, of the kinds which appeared in the coal, cotton and shipbuilding industries between the wars, clearly called for social action, and not for trust either in *laissez-faire* or in the unregulated working of private monopoly. In certain industries, notably those which had lost a substantial part of their export markets and those in which over-expansion during the last war needed to be corrected, some scaling-down was evidently needed; but this was in itself so painful a process that it was strongly resisted. Reliance on the forces of competition to achieve the required results by driving the less efficient, or more disadvantageously placed, firms out of the market was by no means satisfactory;[1] for it was very slow and resulted in what was known as 'weak selling'—that is, in selling under cost by firms which were ready to incur long-run losses if only they

[1] It was by no means always the technically least efficient firms that were driven out; for some of the more efficient in a technical sense had got themselves into a financial jam which led to their elimination in favour of concerns which were less efficient in a technical sense.

could accumulate liquid cash to tide them over their immediate difficulties. Firms which ought, theoretically, to have been eliminated clung on to life; and when the situation became intolerable, the outcome was the creation, with or without State support, of sanctioned monopolies which shared out the trade among the survivors on terms which often led to excessive costs. This happened because the sharing-out was generally done by allocating to each firm a quota of production which did not allow it to operate at *optimum* level, or, where it did, compelled it to pay fines to its competitors as penalties for exceeding its quota. Such cost inflation led inevitably to a restriction of total output below the level which could have been profitably maintained by the more efficient firms, and thus increased unemployment yet further.

Some scaling-down was necessary in the industries affected by failure of foreign demand; but in practice the scaling-down was either by too much or by too little. Moreover, the scaling-down ought to have been accompanied by organised measures for the transference of redundant workers to other jobs, including measures of industrial re-training and, where necessary, deliberate establishment of new industries in the areas badly affected. These things, however, could not be undertaken in a situation in which there was unemployment not only in the specially depressed industries, but in others as well; for where were the re-trained workers to find employment, and where could markets be found for the products of new industries, under conditions of general economic depression? The presence of general as well as structural unemployment—that is to say, of cyclical depression in addition to structural maladjustment—made it impracticable to devise effective measures for dealing with the problems of the industries which were suffering from structural maladjustment. The attempts to cope with unemployment in the depressed areas by large-scale transference of labour broke down for this reason: there were in effect no areas suffering from a shortage of labour to which the redundant workers from the depressed areas could be satisfactorily transferred.

If the economy in general had been in a state of 'full employment', it would have been relatively easy either to transfer the workers displaced by structural unemployment to places where the demand for labour was expanding faster than the local supply or to found new industries in the depressed areas. In other words, if there had been no 'cyclical' unemployment, structural unemployment would not have constituted nearly so difficult a problem as it did in fact.

We are therefore led back to the conclusion that, serious as the problem of structural unemployment was between the wars, and may be again after the present war, the clue to dealing with it effectively lies in the handling of 'cyclical' unemployment. If we can effectively prevent the recurrence of a situation in which the total demand for labour is well below the supply, the problem of shifting labour from one use to another will be much less difficult to handle.

'Cyclical' unemployment, we have seen, arises when business men in general take so poor a view of the prospects of profit as to regard a substantial fraction of the available resources of production as not worth using. This attitude on their part, for reasons which have been already explained, is usually reflected in a much sharper fall in the activity of the industries making capital goods than in those which produce consumers' goods and services. This is so markedly the case that, if the demand for capital goods can be kept up, no great difficulty is likely to be encountered in keeping the demand for consumers' goods and services up to the pre-existing level, provided that wages are reasonably maintained. But how is the demand for capital goods to be kept up? One way that can be tried is a relaxation of credit conditions, both by reductions in interest rates and by making loans more easily available to borrowers of doubtful solvency (for their solvency will be in many cases greatly improved if the measures designed to expand employment succeed). This method, however, even if it is abetted by bank action in increasing the available supply of money, may fail if business men are either very pessimistic in their estimates of prospective profit, or very much wedded to restrictive monopoly practices, or highly suspicious of the political colour of the Government responsible for initiating the policy of monetary expansion. If any or all of these conditions exist, attempts to push more money into circulation or to induce additional investment may fail, or at any rate the doses of new money needed for success may be so large that no Government dares venture on them, and accordingly the policy is stopped short before it becomes effective, and the additional money remains unused, or is returned into the hands of the bankers as fast, or almost as fast, as they set it in circulation.

In such a situation, a Government can resort to subsidies in aid of investment. These in their least venturesome form take the shape of loans at low interest rates, or of guarantees for a period of years of the interest on money provided by private investors. In a more advanced form, they can be actual grants, without interest, or even gifts outright to forms of private enterprise which it is desired to encourage. Such methods are, however, in practice very difficult to pursue; for if gifts, or special financial facilities, are given to some enterprises and not to others, the cry is at once raised that the State is weighting the scales unfairly against those forms of business which are not favoured in these ways. There arises always a clamour for the extension of the same favours to more and more claimants; and the interests which do not get them complain bitterly that they are being taxed, or otherwise penalised, for the benefit of those that do. There is, moreover, the question of the methods by which the State is to raise the funds for its subsidies. If it tries to find the money out of increases in general taxation, the effect of the higher taxes may be further to depress business confidence: if it raises the money by loans, which is greatly preferable, the orthodox attack it for living beyond its means and adding to the burden of the public debt. If, finally, it considers merely creating the additional money by its own *fiat*, without paying anyone for the privilege, there goes up a howl from the bankers, who regard themselves as the only persons who are entitled to create money out of nothing, and the result is seen in a loss of confidence by the bankers—a state of affairs which few Governments under capitalism have courage to face.[1]

In theory, the policy of subsidising private investment could be made to work, provided that the Government were prepared to go through with it and to stand up to the vested interests which would either oppose it or clamour for a wider and indiscriminate extension of it to cover all claimants. It could work, provided that taxation could be so levied as to fall mainly on attempted savings which were not being invested, or that it was financed by borrowing at reasonably low interest rates or by the issue of *fiat* money, and that market rates of interest were not allowed to rise as a consequence of the entry of the Government into the field. In practice, however, nothing is more unlikely than that these conditions will be satisfied. On plea of the necessity of impartiality, the Government will be driven to concede subsidies to businesses that do not need them as well as to those that do—at any rate within the same industry, if not over industry as a whole. Taxation cannot in practice be levied in the way required. Unless the Government is in fully effective control of the banks, it will not be able to prevent its policy of borrowing from causing interest rates to rise, and it will not be allowed to supply the funds it emits by issuing *fiat* money without paying toll to the bankers. Of course, these considerations do not prevent Governments from paying out subsidies in particular cases; but they are likely to prevent any Government under capitalist conditions from carrying a policy of subsidies to anywhere near the point to which

[1] For a further discussion of the effects of State creation of money see page 119.

it would have to be carried in order to offset a major depression. They are, moreover, of such a kind as to make it probable that such subsidies as are given will be very wastefully applied.

If the trick cannot be done by the mere emission of additional bank money or by Government subsidies in aid of investment, what remains? The remaining remedy is the undertaking by the Government itself, or by local authorities or other public bodies acting under its auspices, of extensive public works. Public works are, of course, investment just as much as works instituted under private auspices. The amount of investment incorporated in a power station or a harbour is exactly the same whether it is built with public or with private money, or to the order of a public or of a private body. A deficiency in private investment can be made good by an expansion of public investment, or private investment can be, in the normal working of the economic system, replaced by public investment to any extent. Public, equally with private, investment is a direct cause of employment in the industries producing capital goods, and also an indirect cause of employment in the industries on whose products the persons directly employed choose to spend their incomes. If it is argued, *a priori*, that State works are always wastefully and expensively executed, this does not invalidate the argument. Indeed, the more wasteful and expensive they are the more labour will they employ and the more indirect employment will they create. This is not a defence of wastefulness; for the more waste there is the less useful capital goods will the public get for its money. But to the extent to which the object is employment, the wastefulness will not matter until a state of 'full employment' is approached. Then it will matter; for the State works will then begin to absorb labour which could be more usefully employed elsewhere, and the total wealth of the community will be plainly less than it could be. I am not at all defending wasteful public works, or accepting the contention that public works are of necessity wastefully carried out. But I am saying that, even if they were, this would not prevent them from achieving the purpose of increasing the volume of employment; and I may add that even the most wasteful public works could hardly be so wasteful as the practice, to which we have been addicted hitherto, of paying men doles for doing nothing for years on end instead of setting them to work.

CHAPTER VI

PUBLIC WORKS

By 'public works' are meant works of capital construction carried out on the initiative of the State or of other public bodies, and paid for either out of public funds or out of funds borrowed by public bodies from private persons. Public works can be, but need not be, carried out by the method of 'direct employment'; they can equally be carried out by private contractors working to the order of public bodies. The essence of them is that the State, or some other public body, gives the orders to execute them, and owns them when they have been executed, in the sense of controlling their use. In a sense, they may even be owned privately, as are the properties of the Central Electricity Board and the London Passenger Transport Board, which belong finally to the owners of bonds or shares in these undertakings. If the State floats an undertaking and retains in the last resort control over it and power to direct its policy, the works carried out under its auspices can reasonably be regarded as 'public works', even though they may be financed with money borrowed from private investors.

Public works, in the sense in which the words are now currently used, are to be distinguished sharply from 'relief works'. The difference is that public works, whether the public body acts directly as employer or uses a contractor to carry them out on its behalf, are executed by calling upon the services of the persons best able to carry them out, and are paid for at ordinary commercial rates. Relief works, on the other hand, are works instituted for the purpose of taking on unemployed labour, whether or not it is the kind of labour most suitable for the job, and are usually so designed as to absorb directly as much labour as possible in conjunction with as little as possible of other productive resources. In the case of public works, the object is always to produce something useful at a reasonable cost: in the case of relief works, the value of the product is often a quite secondary consideration, and cost is considered only in the sense that an endeavour is made to employ as many persons as possible at the smallest possible *total* cost. On public works, labour is engaged in the ordinary way, through the labour market, and no exclusive preference is given to persons who are out of work: on relief works only the unemployed are taken on. On public works labour is paid for at standard rates of wages: on relief works often all that is paid is just enough to keep the employed workers from physical destitution.

In effect, relief works are designed to give work of a sort—almost, of any sort—to unemployed persons in preference to maintaining them on doles; whereas public works are designed to bring about an expansion in the total volume of regular and useful employment, rather than to employ any particular individuals. In practice, of course, the distinction is not hard and fast. The British Government during the depression made some of its assistance to public works conditional on the contractors taking on a certain proportion of men who were out of jobs—especially workers from the depressed areas who had been long unemployed. This produced a hybrid type, betwixt and between 'public works' and 'relief works'; and it did not work well. The United States Government, faced by a much stronger prejudice than existed in Great Britain against 'doles', and unequipped with any system of Unemployment Insurance, resorted on a large scale to 'Work Relief' as well as to 'public works' proper, and showed considerable ingenuity in devising forms of 'Work Relief' especially for unemployed black-coated workers. This resulted in some interesting social experiments, including public theatres run by unemployed actors, until they were shut down by the protests of private capitalists against 'unfair competition'. In general, however, relief works have shown themselves thoroughly unsatisfactory. They usually result in bad, and often in unwanted, work carried out at high cost. It is immeasurably better, where it can be done, to stimulate ordinary employment, including employment on public works proper, to such a point that the unemployed are absorbed in the jobs for which they are most suited, instead of being segregated upon types of work for which many of them are thoroughly unfit.

The question is, How much can be done by State action to stimulate employment by way of public works, under an economic system dominated in general by capitalist forms of business? The first reaction of old-fashioned orthodoxy is to maintain stoutly that nothing at all can be done, on the ground that any investment embarked on by the State will be completely countered by a corresponding fall in private investment. This used to be known as the 'Treasury View', in the days before Lord Keynes had found his way back into Whitehall. It found expression, in the crudest possible form, in a White Paper issued by the Treasury in 1929 in answer to those who were contending for an active Government policy designed to combat unemployment. The Treasury at that time argued quite simply that any kind of public works, which it was assumed would be financed by borrowing, would necessarily drain away so much money from the capital market, and therewith bring about an equivalent reduction in private investment.

The assumptions behind this view seem laughable to-day; but let us not forget that they were seriously made, with the full authority of the Government behind them and with Mr. Churchill as Chancellor of the Exchequer, as recently as 1929. They were, first, that there is a fixed capital fund; secondly, that the whole of this fund is bound to be invested in capital works, either by private persons or by the State; and thirdly that, this being the case, no action by the State can influence the volume of employment, at all events if it takes the form of public works financed by borrowed money. Lord Keynes, in his published answer to the Treasury Memorandum, correctly pointed out that the Treasury view, if it were accepted, would have to apply to private as well as to public investment, and that accordingly the Treasury ought to look as much askance at any private capitalist who proposed to raise money for building a new factory as at any politician who proposed to build a new road or housing estate under public auspices. If the sum-total of capital available for investment is absolutely fixed, and if the whole of this fund is bound to be actually invested, clearly there is no point in the State attempting to substitute public for private investment as a means towards further employment. If . . . if . . . ; but what person in his senses can believe that either of these suppositions fits the facts? The 'Treasury View' is nonsense.

What, then, can have possessed the clever gentlemen at the Treasury to talk such rubbish? What they meant, as distinct from what they wrote, was that all public works would either compete with private enterprise, and thus reduce the willingness of private capitalists to invest, or waste on uneconomic forms of construction money which could be better devoted to other uses. They were opposed to any increase either in taxation or in the public debt for the promotion of public works: they were opposed to the State spending *on anything* more money than it absolutely had to spend. They believed that the only effective way of restoring the level of employment was to increase the confidence of business people in the prospects of profit, and that any extension of State action in the field of public works would undermine this confidence. They did not want public bodies to build a lot of houses, because they regarded such action as trenching on the sphere of private, profit-making enterprise. They did not, however, wish to make plain, perhaps even to themselves, the extent of their politico-economic bias; and accordingly they had to cover up what they really had in mind with a specious show of theoretical inexorability. They cannot really have believed that there was a fixed capital fund, which was all of necessity actually spent on capital goods; for, if they had believed this, they could not have believed in the possibility of any sort of economic recovery. They lied, as people so often lie, in the assurance of being right in their conclusions and therefore justified in backing them up with any arguments they could find, no matter how nonsensical, if they could but be made to look plausible.

For the same reasons as caused such pitiful nonsense to be talked by clever men, quite a number of other persons, clever as well as foolish, took these arguments quite seriously. Anyone who was opposed to State enterprise because he feared that it would limit the scope for private enterprise or interfere with the practices of private business, fastened eagerly on the Treasury arguments, and made them his own. The Treasury got away with it; and even the Labour Government which came into office in the same year (1929), though it professed to see through the Treasury nonsense, did nothing to stand out against it in practice. As the world slump came on, Government and Treasury alike elected to pour out more and more money in doles to the unemployed rather than to embark on any extensive public works. Moreover, such small works as they did embark on they were apt to taint with conditions which assimilated them partly to relief works, both by insisting on the engagement of long-unemployed men and by selecting for preference such works as would employ the largest amounts of direct labour at the smallest total cost.

We can dismiss without further parley the 'Treasury View' that public works can achieve no addition to the volume of investment because there is a fixed capital fund that is bound all to be used in the absence of any action by the State. Can we dismiss as easily the view that public works will not in practice increase the volume of employment because, by undermining the confidence of business men, they will cause elsewhere more unemployment than they provide employment? Not quite so easily; for it is not impossible for such a situation to arise, if business men are obstinate enough in their hostility to public economic enterprise, and if the Government is *not* persistent enough in standing up to them. There can be such a thing as a strike of capitalists—a refusal by business men to invest money in production on account of their hostility to the policy of the Government in power. Such strikes undoubtedly occurred in the United States when, in the course of the New Deal, President Roosevelt set about trying to reform the habits of American capitalism by restricting stock market gambling and by controlling the activities of public utility corporations, limiting the powers of holding companies, and so on. It was true for a time that the more money the United States Government poured out on public works, the more American big business drew in its horns. British capitalism showed signs of reacting in a somewhat similar way when it had made up its mind to get rid of the Labour Government in 1931.

In the American case there were complications. The American big business world was practically at one in opposing President Roosevelt's attempts to reform the working of American capitalism, and also in resisting forms of public works, such as the Tennessee Valley Authority, which it regarded as invading the sacred field of private enterprise. It was not, however, at one in opposing the President's recovery policy as a whole; for its difficulties were much too serious for it not to want all the help it could get in combating them, short of sacrificing any of its privileges. Accordingly, American big business wanted the Government to pour out money in assistance to private enterprise, and was not opposed to forms of public works which it did not regard as invading the sphere of its own profit-seeking operations. It valued such works as adding to the volume of purchasing power available for buying their products; but it demanded that they should be kept strictly to forms which would not compete with any kinds of private enterprise with which it was concerned.

It is, however, evident that, the narrower the range of activity within which the State is allowed to operate in promoting public works, the greater is the danger both of failure in achieving what is needed in the expansion of employment and of providing the community with the wrong sorts of capital construction. Suppose, for example, the State is allowed to promote public works with the object of increasing investment and employment, but only on condition that it limits itself strictly to providing things which private enterprise does not in any case set out to provide. The State, either directly or through the local authorities or other agents, will be able to provide roads, bridges, town halls, hospitals, elementary schools, post offices, and a few other types of capital construction; but it will be able to do nothing directly to correct structural maladjustments in industry, to improve transport facilities, to make power supplies more easily and cheaply available, to build houses, or to place additional goods of any sort on the market. Even water-supply projects will arouse the opposition of privately owned water companies; and even the building of secondary schools may be regarded as an act of hostility to the 'public' or to the numerous private schools.

No doubt, many of the things the State will be allowed to provide, even under these limiting conditions, are well worth having. But if the entire programme of public works is to be concentrated upon such things, there will be a serious danger that the provision of them will advance a long way ahead of the provision of other things that are equally needed, but are taboo from the standpoint of public enterprise; or, alternatively, that the State, having provided only fairly small quantities of these things, will stop short altogether for fear of outrunning the *relative* need for them as against the other things which it is not allowed to provide. It will have to meet, in each of the fields in which it is allowed to operate, the hostility, not of business men as such, but of the 'economisers'—of those who want to cut down public expenditure in general, and especially expenditure on what they regard as unnecessary luxuries. This opposition will be particularly strong on many of the local Councils through which in practice the State will have to carry through most of its public works within this restricted field. The result will be that either the State will provide too many of the things which it finds that it can provide with least opposition (e.g. roads), or it will not provide enough of anything to make any serious impression on the unemployment problem, and its failure to do this will thereupon be quoted as a demonstration of the ineffectiveness of 'public works policy'.

It is, indeed, necessary to realise that small doses of public works are not in the least likely to make any noticeable impression on the volume of unemployment if they are set on foot during a major slump. The fluctuation in the volume of investment between good and bad times is not a mere matter of a few millions. It runs into hundreds of millions. According to Colin Clark's estimates, the volume of gross investment in Great Britain (including renewals and replacements) fell from £682 millions in 1929 to £414 millions in 1932. In the United States the fluctuation over the same period was enormously greater, not only absolutely, but in proportion to the volume of economic activity as a whole. Gross investment in the United States has been estimated at 34½ billion dollars in 1929, and at less than 8 billions in 1932.[1]

Of course, it is not suggested that the State will be called upon, in order to promote full employment, to fill up the whole of this great gap. The expectation is, not merely that private investment will not fall off as public investment proceeds, but that it will increase as the public investment improves all-round prospects of profits by adding to the volume of current purchasing power. How much of the gap the State will have to fill will depend on the readiness with which business men respond to this stimulus; and this in turn will depend on their mood, as well as on the real increase in purchasing power resulting from the State's activities.

[1] British figures from Colin Clark's *National Income and Outlay*, U.S.A. from S. Kuznets, Bulletin 52 of the National Bureau of Economic Research, quoted in Keynes's *General Theory of Employment, Interest and Money*. The corresponding totals for net investment, from the same sources, are, for Great Britain £314 millions in 1929 and £29 millions in 1932, and for the United States 25½ billion dollars in 1929 and just over one billion in 1932.

If their mood is one of hostility to the Government, they will be much the less ready to respond to the objective stimulus of increased purchasing power. They will be hesitant and suspicious, and, in the extreme case, will even neutralise a moderate policy of public investment by intensifying their own refusal to invest. If the Government persists in its policy—if it is strong and self-confident enough to be able to persist—this mood will pass; for beyond a certain point business men will not go on cutting off their noses to spite their faces. When Government spending on public works reaches a scale on which there are clearly large profits to be had for the picking-up by private investors in new enterprises, the private investment will take place, even if it is accompanied by a great deal of grumbling. But, if business men are in a bad mood, it may take a really tremendous programme of public works to break down their resistance. It follows from this that Conservative Governments, where they are prepared to go in for public works at all, can usually achieve a given result with much less public expenditure than Governments of the Left. The business men feel more confidence in them, and therefore come in more readily to play their part in filling up the gap.

Naturally, Conservative Governments are also scrutinised less closely when they resort to forms of public works which to some extent invade the field of private enterprise. The Baldwin Government was able to pass the Electricity Act of 1927 with much less opposition than would have been encountered if it had been put forward by a Labour or a Liberal Government. There were capitalist interests—above all, the suppliers of electrical equipment—who wanted the 'Grid'; and the private Power Companies, which would have preferred to get the whole business into their own hands, but realised the political impossibility of doing this, were prepared to arrange a deal with the Conservatives, who were certain to do their best for them, whereas they would probably have fought the whole Bill if it had been brought in by a Government they disliked. This, no doubt, was not a case of public works instituted mainly for the purpose of raising the level of employment, though this was one of its objects; but the issues at stake between public and private enterprise are essentially the same.

The scale on which the State needs to act in order to increase or to maintain the level of investment is affected, not only by the attitude of the business world to the Government in power, but also by the stage at which a policy of public works is put in operation. The aim of those who see in public works a vitally important instrument for the control of economic fluctuations is not merely to correct them after they have happened, but rather, as far as possible, to prevent them from happening. When a depression has actually gone some way, the confidence of the business world in the prospects of profit is bound to be low, and the dose of public works needed to promote recovery is bound to be big, even if the political conditions are favourable. If, on the other hand, a programme of public works can be held ready to be put into actual effect promptly on the first sign of the onset of depression, a very much smaller dose is likely to be effective; for business confidence can then be prevented from declining, and any stimulus applied to purchasing power will produce an immediate and decisive effect.[1]

The *timing* of public works is indeed a matter of crucial importance. Any sound programme is bound to take a considerable time to prepare, not only from the technical standpoint, but also because difficult and prolonged negotiations with local authorities, and sometimes with private interests as well, are involved. Improvised programmes, set on foot in a hurry in order to provide immediate employment, are bound to be ill-considered and wasteful, and to give rise to endless trouble with those who have not been sufficiently consulted in advance. The right course is for the Government and its agents to have always in readiness a large number of projects, fully worked out in consultation with those concerned. It can then decide, when the right moment comes, with which of these projects to proceed at once, the number selected depending of course on the scale on which it appears necessary to operate in order to prevent depression from taking hold. This question of 'timing' will be discussed further at a later stage: my point here is that the more promptly the State can take action at the first sign of recession, the less action it is likely to have to take.

If action is needed on any considerable scale, it is important that public works shall be allowed to be set on foot over a wide field. A public works policy that is confined strictly to types of work which will not be regarded as in any way trenching on the field of private enterprise, and will not be objected to by anybody on this ground, will very soon run into difficulties, and will, in any event, be unable to provide sufficiently diversified forms of employment. It will, in addition, be faced with the difficulty that the types of work permitted will be needed most in expanding areas, where there is comparatively little unemployment; so that either work will be provided when it is less needed, or buildings

[1] A stimulus at this point to consuming power directly, by the provision of credits to consumers, would of course have the same immediate effect, unless it aroused fears of 'unsound finance' of such a nature as to disturb business confidence. For a discussion of this problem, see pages 151 ff.

etc. will be erected where they are less needed, or even not needed at all. If the public works are carried out in the expanding areas, there will be the problem of persuading labour to migrate from the more depressed districts in search of work; and this will be the case most of all where the depressed areas are dominated by industries, e.g. exporting industries, which will not be stimulated as much as others by a general revival of demand brought about by the expenditure on public works. The more the State is able to diversify its provision and to spread it about the country, without being driven to forms of works that are not really wanted except for the sake of the employment they provide, the more successful the policy is likely to be in stimulating a general revival of enterprise.

Public works, where they are undertaken at all, are not in practice limited so narrowly as to exclude all forms of production in which they may be held to be competitors of private capitalism. Exceptions are made—for example, in the case of house-building. But even in this case there are always powerful interests on the alert to restrict the scope of public building by municipalities or other agents of the State. Until after the last war, the provision of houses by public authorities was on a very small scale. The vast arrears of house-building which had accumulated by 1919 forced the State, through the local authorities, to enter the field to quite a considerable extent. But there was, throughout the inter-war period, a continual tussle between those who favoured an extension of public building and those who wished to confine it within the narrowest possible limits. The Chamberlain Housing Act of 1923 was designed to restrict public building by substituting subsidies to persons who would undertake to get houses built under private ownership: the Wheatley Housing Act of 1924 was designed to extend the range of municipal building. After the fall of the first Labour Government, an attempt was made to return to the Chamberlain methods; and then the Greenwood Housing Act, passed under the second Labour Government, was an attempt to tip the balance back the other way. During and after the great depression of the 'thirties, the Conservatives did all they could to limit public building to slum-clearance schemes and other special types of scheme, and to leave the main body of house-building to be carried on by speculative builders working in alliance with Building Societies and Insurance Companies. There was no consistent policy: it all depended on the political complexion of the Government that happened to be in office.

Side by side with this major tussle between private and public enterprise in the field of house-*ownership*, there was a minor tussle between the advocates of building through private contractors and those who favoured 'direct employment' by the public bodies concerned. 'Direct employment' meant cutting out the private master builder, and putting the actual building operations under the control of a Borough Surveyor or other local government official. Building through contractors meant using the services of the ordinary master-builders but relieving them of their speculative functions as house-salesmen. By far the greater part of the public building done between the wars was carried out in this latter way, through private contractors; and the same policy has been consistently followed in the conduct of building operations during the war. Even Labour Councils made large use of contractors for carrying out their housing programmes, partly no doubt because municipal building aroused much less opposition from vested interests when the master-builders were allowed to do the work on a profit-making basis.

From the standpoint of 'public works policy' as a stimulus to general economic activity, it is not of fundamental importance whether the work is done by direct employment or by private contractors. Provided the employment occurs, it does not matter, from this point of view, who the actual employer is. But it does matter very much whether or not the State is prevented from taking the responsibility for carrying through housing schemes outside such special fields as slum-clearance. The reason why little opposition is offered to State action in slum-clearance is that such work nearly always involves a loss and does not get done at all unless it is aided by public subsidies. It is not, therefore, really competitive with private enterprise, except when the public bodies responsible for it resort to the method of 'direct employment'. Where they use contractors, they are actually putting into the hands of the private building firms work which private enterprise would not be prepared to undertake. But as soon as the State steps outside the field of slum-clearance, and sets out to build houses for the general population, the question of competition, not only with private builders but also with Building Societies and Insurance Companies, inevitably arises.

Stress is laid here on building, and on house-building in particular, because building activity forms so large a part in normal times of the total activity in the field of capital construction. It has been estimated that the work done by the building industry constituted in the 'thirties approximately two-fifths of the total capital expenditure, including replacements and renewals. Accordingly, the extent to which the State is free to operate over the greater part of this field will clearly be one of the main factors in determining the efficiency of 'public works policy' in stimulating investment and employment.

To this argument the opponents of State economic enterprise, even in those forms in which the actual work is carried out through private contractors, will reply that employment will be stimulated fully as much if the building is done to the orders, not of public bodies, but of private persons. They will therefore favour, as Mr. Chamberlain did in the 'thirties, any policy which will stimulate private building while keeping the State and the local authorities out of the field. In the 'thirties, this was largely accomplished, with the aid of the Building Societies and Insurance Companies. The greater part of the houses built during and after the great depression were erected without the intervention of any public body. This was made possible by the sharp reduction in long-term interest rates which came about during the depression and was thereafter maintained deliberately by agreement between the Government and the Bank of England. If long-term interest rates were low, it was possible for houses to be built in large numbers without subsidy, as long as there were purchasers who could afford to spend substantial sums on house-room and to put down an appreciable capital sum towards the cost of buying a house. To such persons the Building Societies and Insurance Companies were ready to advance the balance of the purchase-price, to be repaid on the instalment plan; and, with such purchasers in the offing, speculative builders could readily obtain such working capital as they required. In order to aid this process, Building Societies were encouraged by highly preferential arrangements in respect of taxation, and were enabled to accumulate huge funds from deposits made largely by members of the middle classes. The total result was not that the house-buyer on the instalment plan got his house at a low interest rate; for the Building Societies and Insurance Companies charged him substantially for the financial accommodation. But the price was lower than it would have been if market interest rates had been higher; and there was a big boom in private house-building which served the Conservative Governments of the 'thirties in good stead as a substitute for public works under the auspices of the State.

The opponents of public enterprise would dearly like to see this happen again in the period after the present war. It is, however, most unlikely to happen. Only a limited section of the population—mainly the better-off black coats and a small upper stratum of the most skilled manual workers—could afford to buy houses on the instalment plan at the prices at which they could be offered with the aid of finance provided by the Building Societies and the Insurance Companies; and most of these persons had bought their houses before 1939, when the majority of them were still engaged in paying off their mortgages. There is certain to be, after the war, a large supply in the market of second-hand houses of this type; and it can be taken as certain that there can be no renewal of the building boom of the 'thirties, in the form which it then assumed. Most of the post-war demand for new houses will be for houses to be rented at reasonably low rents, rather than bought on the instalment plan; and even purchasers who are prepared to buy by instalments will be mostly too poor to afford the prices which purchase through Building Societies or Insurance Companies involves. There will, moreover, be little prospect of a further fall in long-term interest rates such as occurred in the 'thirties; for, during the present war rates have been kept low by Government and banking policy, and there is not much room for a fall.

Accordingly, if there is to be a big house-building programme after the war, the prices or rents to be charged for the houses will have to be kept low. This cannot be done at all unless those who rent or purchase houses are given the full benefit of the lowest practicable interest rates. This means that the State and the local authorities, which can borrow money on the best terms, will have to pass on this advantage directly to those who need the houses, instead of leaving them to pay the higher rates which are involved in allowing a margin to Building Societies or Insurance Companies to cover their working expenses *plus* a profit. This, however, cannot be done unless the State or some other public body assumes the direct responsibility for getting the houses built, and for letting or selling them to those who need them. In all probability, it will not be enough thus to give the consumers of house-room the benefit of the lowest practicable interest rates. Actual subsidies for house-building will probably be needed as well, at any rate during the years immediately after the war. But the amount that will have to be spent in subsidies in order to provide houses at rents or prices which consumers can afford to pay will be very much smaller if interest charges are kept as low as possible than if they are allowed to be inflated by intermediate charges.

It follows from what has been said that the great bulk of post-war house-building will have to be carried out under public auspices, if houses are to be made available, without inordinate subsidies, at rents which ordinary people can afford to pay. This necessity, it will be seen, has nothing directly to do with the need for a policy of public works designed to establish and maintain a condition of 'full employment'. An extensive programme of house-building will, of course, be helpful, equally with any other measure which will increase 'investment', in stimulating employment. But the need for houses, in view of the arrears of building during the years of war, the loss due to bomb damage, and the necessity of extensive re-planning of towns, relocation of populations, and improvement of rural housing standards, will for some time be so great as to strain to the utmost the capacity of the building industry, even if active steps are taken to enlarge it by training additional skilled workers. The necessity of working in any case up to full capacity will make it impossible, for some time after the war, to use building as an instrument for combating *cyclical* unemployment, for an industry which is already working under full strain cannot be further expanded quickly in order to offset a tendency towards depression in the economic system as a whole. Building is destined to account after the war for a considerable proportion of total investment and for a still larger proportion of State-financed investment. But its amount will be determined mainly, not by the requirements of a policy of 'full employment', but by the absolute need for more and better houses.

We have, then, even if the State acquires full freedom to operate in all forms of house-building, either by using contractors or by the employment of 'direct labour', to look elsewhere for the types of public works which can be accelerated or decelerated according to the requirements of a policy of 'full employment'. For this purpose, the State needs to have ready projects which can be put in hand sooner or later according to the general condition of employment in the country—projects which are worth carrying out some time, but are not of such a nature that their execution cannot be deferred. At all events, it needs a large reserve of projects of this order, over and above such projects as are meant to be instituted irrespective of the fluctuations expected in the level of total employment.

At this point, it is imperative to get clear about the distinction between two essentially different purposes which 'public works policy' can be called upon to serve. If the economic system as a whole oscillates between a condition of practically 'full employment' and one of substantial underemployment, public works, for the purpose of maintaining employment, need be invoked only in bad times, and only up to the point to which they are needed for keeping employment continuously up to the level which it actually reaches in good times. If, on the other hand, a condition of 'full employment' is not reached even in good times, it becomes necessary to invoke public works in good and bad times alike (though of course on a larger scale in bad times) in order to remove an endemic failure of the economic system to make full use of the resources available for employment. In other words, if there is, under the prevailing economic arrangements, a permanent surplus of labour, public works can no longer be regarded simply as a balancing factor: they are needed to induce a fuller use of resources than can be achieved if, except in bad times, the economy is left to look after itself, without active intervention by the State.

It is an undisputable fact that Great Britain, between the two wars, was suffering not only from serious cyclical fluctuations in the demand for labour but also from a permanent deficiency in the demand. In order to set this right, the State ought to have intervened to increase employment in relatively good years as well as in periods of relative depression. The form which this intervention ought to have taken in the relatively good times need not have been the same as was appropriate for combating cyclical depression; for the unemployment which continued to exist even when demand was relatively high was not due to the same causes as much of the unemployment which was added to it in the bad years. The main causes of endemic, as distinct from epidemic, unemployment were to be found either in the structural maladjustment of the economic system in face of changing techniques, demand preferences, and conditions of external trade, or in the practice of monopoly in damping down production in order to maintain prices and profits. These two factors prevented 'full employment' from being reached even when the circumstances were relatively favourable. Cyclical additions to unemployment, on the other hand, while they might be aggravated by structural defects and by the behaviour of monopolists in bad times, were mainly due to more general causes affecting the economy as a whole—causes which have been fully enough discussed in previous chapters.

Under these circumstances, which seem likely to recur after the war—probably in an aggravated form—in the absence of corrective public policies, there will be a double need for public works. One part of the public works programme, in which house-building will occupy a position of key importance, will have the function of increasing the level of employment in good and bad times alike, and will not need to fluctuate according to cyclical up-and-down movements. A second part of the programme will need to have a definitely 'counter-cyclical' character and purpose, and to consist of projects which can be advanced or delayed according to the general prospects of employment in the economy as a whole.

It is not, of course, suggested that the State need limit its economic activity to measures falling under either of these heads. It may, for other reasons, be desirable for the State to extend the range of public enterprise far beyond what is required for the maintenance of 'full employment'. It may be desirable to socialise all industries, or all major industries, or quite a number of industries, for reasons which have nothing to do with the maintenance of employment at a satisfactory level. That is a quite different question, which I am not now attempting to discuss. It is, in effect, the entire issue between Socialism and private enterprise. To the argument with which we are here concerned this issue is quite irrelevant.[1] This book is not about the case for Socialism against capitalism: it is about the steps which are necessary for maintaining 'full employment' in a predominantly capitalist society—if it is possible to maintain it in such a society. The point in this argument which we have so far reached is that it may be necessary, for this purpose, for the State to engage in public works not only for the purpose of countering cyclical depressions, but also for that of meeting a persistent tendency of capitalism in its twentieth-century form to make less than full use of the productive resources which are at its disposal. These two kinds of 'public works policy', I have argued, may need different methods. In what respects the appropriate measures will need to be different we must next proceed to inquire.

CHAPTER VII

STRUCTURAL READJUSTMENT

THE COMBATING of cyclical unemployment is primarily a matter of raising the *total* demand for labour, and of other productive resources, rather than of applying measures specifically designed to raise the demand for resources of particular kinds. In general, it can be assumed that an increase in the total of effective demand will distribute itself over the main part of the economy, apart from those sections of it which are suffering from serious structural maladjustment. This is, no doubt, more completely true of the indirect than of the direct effect of State intervention by means of public works. The direct employment provided by such works will depend on what they are: the indirect effect will spread itself out over the entire economy as the recipients of incomes from the public works spend these incomes on whatever they feel like buying. It is therefore of importance that 'counter-cyclical' public works projects should be *well spread*, both industrially and geographically; but, provided that they are well spread, it does not much matter what forms they

[1] For a discussion of this wider issue see my *Great Britain in the Post-war World* (Gollancz, 1942) and my *Fabian Socialism* (Allen and Unwin, 1943).

take, if they are being considered exclusively from the standpoint of their counter-cyclical effects. It does, of course, matter a great deal, for other reasons, that they be well-chosen, so as to yield to the community the largest return. But even if they are ill-chosen, this will not prevent them from producing their immediate counter-cyclical effect.

The position is quite different when we come to consider public works instituted with the object of offsetting an endemic tendency towards underemployment of the available resources. Such works must be directed purposively towards correcting the faults in the economy which are responsible for this tendency. They must be directed, that is, to the two main objects of correcting structural maladjustments and of countering monopolistic restrictions. Accordingly, they must be designed to increase total employment by increasing particular kinds of employment. They must pay particular regard to the specific character of the resources which remain unemployed or underemployed in good times as well as bad; and they must be aimed either at increasing the use of these particular resources, or at the transference of any surplus over what can be used to good purpose to alternative forms of employment.

The State's powers of intervention for the purpose of combating cyclical unemployment need to be wide and general; for combating endemic unemployment the State will need narrower, but further-reaching, powers. It is not, of course, in practice necessary to draw a hard-and-fast distinction; for there are many kinds of public works which can equally well serve either purpose. The distinction is, however, important; and it is necessary to bear it continually in mind.

Public works designed to cure structural maladjustments in the national economy, or to counter other endemic tendencies towards under-use of the available productive resources, will need to be applied continuously, for as long as these tendencies exist. They may be applied with any of a variety of objects among which the following are of outstanding importance:—

(*a*) to modernise an industry which has fallen behind in technical efficiency or administrative organisation, especially when such an industry has failed for some time to set its own house in order;

(*b*) to expand an industry or service more rapidly than it is actually expanding of its own accord, especially where such expansion requires forms of investment which are either difficult for private enterprise to undertake, or would be likely to lead to monopoly if they were undertaken by private bodies;

(*c*) to develop forms of production which are regarded a too risky by private enterprise, because of the risk of capital obsolescence where processes are still at an experimental stage, or because of the uncertainties of foreign competition, or again because the returns are likely to be too long deferred to attract private investors;

(*d*) to experiment in new techniques of production;

(*e*) to provide opportunities for new businesses set up to experiment in new techniques to start with as little capital of their own as possible, and, in general, to help business men of enterprise who are short of capital to enter into suitable forms of production on favourable terms;

(*f*) to extend the supply of services which are regarded as unsuitable for supply by private, profit-seeking agencies, and are already, as far as they exist, largely or exclusively in the hands of public bodies;

(*g*) to regulate the rate of contraction in industries which are suffering from an unavoidable diminution of the demand for their products, in such a way as to limit the amount of contraction by cutting out waste and thus reducing costs;

(*h*) to establish State productive agencies, in industries carried on mainly by private firms, in order to furnish a check on private costs or monopolistic practices;

(*i*) to make special provision for employing the labour of partially disabled or incapacitated persons, where such persons are most likely to be useful if they are employed under special conditions;

(*j*) to establish special Public Corporations for carrying out large projects of developments which are unlikely to be tackled effectively by existing agencies, either public or private.

Let us now try to put a little flesh on the bones of these ten aspects of 'public works policy' which the State may decide to set on foot as remedies for endemic, as distinct from epidemic, unemployment.

(*a*)

to modernise an industry which has fallen behind in technical efficiency or administrative organisation, especially when such an industry has failed to set its own house in order.

I have in mind here such industries as coal or cotton, which persistently refused between the wars to undertake measures of reorganisation that were clearly required. If industries are in a state of inefficiency, this is bound to mean that the *real* costs of the marginal firms in them (probably, in fact, of most firms) are unduly high. High marginal *money* costs mean at any rate in the long run excessive prices, and therefore restricted sales and employment capacity. No doubt, in such industries, *money* costs are sometimes reduced by cutting wages; but the effect of this is to present windfall profits to the more efficient firms, and also to lower the purchasing power of the workers employed, and thus restrict consumers' demand. The community loses either way—whether the high *real* costs are or are not accompanied by high *money* costs. Where *money* costs are high because of inefficiency a reduction of the *real* costs will bring them down, and thus expand demand and employment in the industry concerned. Where *real* costs are high, but *money* costs have been kept low by wage-cutting, reduced *real* costs will enable wages to be restored, and the increase in purchasing power will increase employment over industry as a whole.

The State can act in such cases either by taking over the entire industry and transferring it to a Public Corporation, on the lines of the Central Electricity Board or the London Passenger Transport Board, or by taking over a part of the industry (where there is some key section of it that specially calls for reorganisation), or by leaving it in private hands, but making its operations subject to the overriding authority of a public Control Board armed with extensive powers of regulation. An intermediate course is to establish a Control Board, and to give the Board power to take over and operate any part of the industry at its discretion. Which of these courses is best will depend on the circumstances of each case, objectively regarded: which will be adopted (if any) is much more likely to depend on political considerations largely irrelevant to the real issues at stake. Let us, however, assume that the decision is taken on objective economic grounds. The State will become responsible either for modernising the industry itself, and for raising publicly such capital as may be needed, or for ensuring that it is modernised by the private firms which are left in possession. Where private firms are to remain, it will be of great importance to include provision for new firms to enter the industry, in order to prevent ossification. Where the industry is taken over by a Public Corporation, it will be necessary to introduce as much decentralisation as possible, in order to give wide opportunities for diverse experiment in new methods. In either case, the industry will need to be equipped with a *collective* organisation for research, not superseding but co-operating with research agencies maintained by separate units within it. Its affairs will need to be made subject to continuous public scrutiny, in order that it may not merely be made efficient in the first instance, but kept efficient thereafter. It will have to enter into careful arrangements with the educational authorities for the recruitment and training of the labour it requires, and for defining the frontiers between training done in Technical Schools and Colleges and training undertaken by the industry itself. If, on reorganisation, there appears to be a surplus of unwanted labour, the industry will have to arrange with the appropriate bodies for the transfer and re-training of these workers.

This is not the place to enter more fully into the right ways of conducting industries which are either transferred to Public Corporations or put under the supervision of public Control Boards. Our concern here is with employment and public works. Clearly, the amount of public works involved will depend on the form which the reorganisation takes. If the industry is taken over wholly or in part, everything that is taken over will belong thereafter to the realm of public works. Where the industry, or a part of it, remains in private hands, it falls outside the realm of public works, but within the sphere of State influence over the volume of employment which it provides.

(*b*)

to expand an industry or service more rapidly than it is actually expanding of its own accord, especially where such expansion requires forms of investment which are either difficult for private enterprise to undertake, or would be likely to lead to monopoly if they were undertaken by private bodies.

Take the case of the electricity 'Grid'. There is no reasonable doubt that this enterprise was desirable, or that it created additional investment and employment, both directly in its construction and in the industries providing electrical equipment. In some areas it cheapened electric power; in most it increased the reliability of the service; in not a few it made electricity available for the first time. It is, however, clear that the 'Grid' could hardly have been constructed by any private agency. Too many compulsory powers were needed to invade private rights—for example, in placing the pylons. There was the whole problem of settling which generating units were to be allowed to continue as 'selected stations', and which were to be put out of business. There were endless questions of compensation, pricing, and standardisation of frequencies and equipment. No private body, even if it had been given a monopoly of main-line transmission, could have arranged all these difficulties. If the 'Grid' was to be built at all, it had to be built and operated under public auspices the more so because it had to deal with many existing local public bodies already active in the field of generation as well as distribution of electric current.

If the electricity supply industry had been left to be expanded by private agencies, its rate of growth would have been much slower than it has actually been. It would, I think, have grown still faster if the whole business of generation, as well as main-line transmission, had been put into the hands of a Public Corporation, and if the distribution of electricity to the consumers had been reorganised under a series of regional public concerns. But what was done did increase investment and employment and therewith consumption; and the change was accompanied by an improved quality of service. Much remains to be done; but what was done is an excellent example of the beneficence of public works in speeding up development beyond what could have been achieved had the State stood aside and left private enterprise to find its own level in response to the profit-motive.

Other public utility services, notably gas and water, obviously occur to the mind as likely fields for similar methods of development. Not, of course, for exactly the same methods, because conditions differ for each service. But in each of them there may well be some big expansion which is practicable under public auspices, but quite impracticable as long as the matter is left to private initiative or control.

(*c*)

to develop forms of production which are regarded as too risky by private enterprise, because of the risk of capital obsolescence where processes are still at an experimental stage, or because of the uncertainties of foreign competition, or again because the returns are likely to be too long deferred to attract private investors.

In the case of the 'Grid', the impossibility of doing the job by private enterprise arose largely out of the complications involved in the use of compulsory powers. But there are other cases in which the volume of private investment may lag behind what is needed from the standpoint of the economy as a whole. Take, for example, the problem of making oil from coal, or of producing synthetic rubber. The plant needed for these processes is exceedingly expensive; and there is a considerable risk that, before it is nearly worn out, it may be rendered obsolete by improvements in technique. The private investor, surveying these risks, may be deterred from attempting anything, because nothing can be attempted except on a large scale. The State is in a better position for taking a risk which, large as it may be, is small in relation to the State's total activities. Moreover, the private investor is often deterred because it commonly happens that the pioneer, in losing his own money, carries through the experiments of which subsequent investors reap the benefit. The State can ensure that, if it incurs the costs, it shall, if it so desires, also reap the later rewards. Even if it does not, the State is interested in the prosperity of the economy as a whole, and the benefit accruing later as a result of the early experiments, even if they are immediately unsuccessful, is a benefit to the community, and is therefore not a matter of no concern to the State, as it is to the private investor who loses his money. This is not to say that the State should embark lightly on large-scale operations in processes which are still at an experimental stage. But it is a relevant factor that, where operations have to be on a large scale, it is easier for the State to take the risks and may be quite out of the question for private investors to be persuaded to take them to the extent required.

No doubt, the State can persuade private investors to take risks which they would otherwise shun. It can do this by offering them subsidies; and this may sometimes be the best way. But when it is a question of investment in very expensive plant, the private investor will usually want not only a subsidy, but a monopoly as well. If new processes or industries are to be monopolised, on account of the technical conditions, surely the monopolies ought to be public and not private. A Public Corporation is the best instrument for developing such forms of production.

Or take forestry. It is common knowledge that there has been in recent times an immense decay of private woodlands, which are falling in area and are mostly in a very bad state. Even with the aid of the Forestry Commission, Great Britain did not succeed between the two wars in making good the wastage of timber that occurred during the last war. Afforestation is unattractive to the private investor because of the very long time he has to wait before he can get any return on his money, and the still longer time he has to wait before he can hope for a commercial return. It is true that the experience of the Forestry Commission between the wars is not at all a good advertisement for public works. That was not the fault of the Commission, which was never allowed to operate on an adequate scale, and was again and again subjected to cuts in its estimates in bad times—when by all the sound rules of 'public works policy' its appropriations ought to have been largely increased. The Forestry Commission fell a victim to the Treasury's hostility to 'public works'. It had no adequate autonomy: its grant was in practice made subject to revision from year to year: it had the heart-rending experience more than once of growing saplings ready for planting, and then having to destroy them because by the time they were ready the money for planting had been taken away by a Chancellor of the Exchequer set on 'economy' and 'balancing the budget' at any cost.

This experience should be a warning. Public works and Public Corporations or Commissions must on no account be made subject to Treasury control. There must be a central Planning organ of the State, with its own resources apart from the tax budget, and a status at any rate equal to the Treasury's. To that issue I shall come back in a subsequent chapter:[1] for the present let us merely note that 'public works policy' will never work well as long as it is made subject to a department whose principal concern is with restricting expenditure and not with promoting capital development.

(*d*)

to experiment in new techniques of production.

This heading overlaps with that which has just been discussed. But it covers activities which do not come under the previous heading. The State does already carry on certain research activities of its own, designed to promote the advance of industrial technique. It has its National Physical Laboratory, its Building Research Station, its Forest Products Research Station, its Farm Institute at Rothamsted, and so on; and it also does a little to subsidise research with an industrial or agricultural bearing carried on in Universities, and, through the Department of Scientific and Industrial Research, shares the cost of the recognised Research Associations for particular industries with the firms which contribute to their support. In addition, it subsidises research done by armament firms, particularly in the aircraft industry, and occasionally finds a little money to enable some particular firm, such as Imperial Chemical Industries or the Gas, Light and Coke Company, to try out on a commercial scale some experiment already made successfully in the laboratory. It does not, however, at all regard it as part of its normal business to try out commercially the experiments made even in its own research stations, much less elsewhere. New industries and processes are regarded as falling within the field of private enterprise, and not of public economic activity.

Should this be so? If the State is to assume a responsibility for maintaining the level of employment, by measures directed against both cyclical and structural unemployment, it will be

[1] See page 169.

bound to interest itself actively in exploring new lines of production to replace those which become obsolete or fail to maintain their markets. There is a great deal to be said in favour of public activity in trying out new methods in experimental factories under public ownership and control. This need not involve any monopoly: indeed, it would be open to the State to make its discoveries and improvements fully public, and to allow anyone who pleased to make use of them, and even to go further, and give special help with cheap capital, rentable factories, and research assistance to firms willing to try out new methods pioneered in the State's own laboratories. In some cases the State could try out its own discoveries: in other cases it could get private firms to try them out on its behalf; in yet others it could, while experimenting itself on a commercial scale, throw the chance open to all comers.

This proposal will doubtless arouse keen opposition from persons who will argue that the State is the very last body to attempt anything new, and that private enterprise ought not, in this field more than in any other, to be exposed to 'subsidised' public competition. This is a stupid argument. No one is proposing that the work should be entrusted to ordinary Civil Servants, acting under Treasury control; and surely trying a new process out on a commercial scale is part of the essential research work connected with it, and the State's right and duty to undertake technical research is not questioned—though much too little of it is actually done.

(*e*)

to provide opportunities for new businesses set up to experiment in new techniques to start with as little capital of their own as possible, and, in general, to help business men of enterprise who are short of capital to enter into suitable forms of production on favourable terms.

This is a development of the preceding point. Before the war the State, through the Commissioners for the Special Areas, established in a number of places afflicted by serious endemic unemployment 'Trading Estates', which should rather have been called 'Industrial Estates'. On these Estates, it was possible for small firms to rent, instead of having to expend capital on building, well-equipped factories, adequately supplied with power, transport facilities, water, and other requisites. This was especially useful to firms which were experimenting with new processes, or processes introduced from abroad. Such firms might in the long run wish to build their own factories, and perhaps to leave the Estates, when the success of their processes had been proved, and capital could be borrowed for development on easier terms. What the Estate did was to give them the chance of starting under favourable productive conditions with a much smaller expenditure of capital than they would have had to face in its absence. This was not, of course, the sole function of the Estates, nor was it fulfilled on a large enough scale. But, as far as it went, the results were good.

I should like to see, after the war, a great development of this type of 'Industrial Estate', not only in depressed areas, but all over the country. It is well worth considering whether a number of the huge factories built for war purposes should not be set aside for this use, instead of being scrapped merely because there is no call for their survival as single factories. The State could then make use of these Estates as sites not only for existing businesses cleared out of congested town areas under re-planning schemes, but also for all sorts of experimental new concerns. Inevitably some of these new concerns would fail; but the social and economic consequences of their failure would be modified if their factory buildings could be readily adapted, and their workers transferred, to fresh concerns which would enter upon possession of the relinquished factories. Some would fail; but others would grow big and flourish; and the system would act as a stimulus to economic progress in a different way, helping to get new factories into operation in a variety of places at a low initial outlay which it would be relatively easy to afford. Such methods would in addition provide a supplementary safeguard against undesirable forms of monopoly.

(*f*)

to extend the supply of services which are regarded as unsuitable for supply by private, profit-seeking agencies, and are already, as far as they exist, largely or exclusively in the hands of public bodies.

The development of the main public utility services has been referred to under a previous head. What I have in mind here is the most familiar of all forms of public works—the supply of roads, bridges, drainage services, hospitals, schools, parks, public camps and camping grounds, nature reserves, playing-fields, allotments, swimming-pools, canteens and restaurants, open-air theatres, and a host of other educational, recreational and sanitary services and amenities. It has been pointed out already that, when the opposition of vested interests causes public works to be restricted within a narrow field, there is a danger that works of these types may be put in hand on an unduly large scale, in relation to other capital developments, because they arouse less hostility. This, however, does not mean that they are not needed on a quite considerable scale. No doubt, many of them, though not all, belong to the group of public works which there is no desperate urgency to carry out at once, and which can therefore be made use of in building up a reserve of projects held ready to be put in hand at the first sign of cyclical depression being on the way. This, however, is not true of all of them. In particular, the development of new centres of population or the rapid growth of existing centres is generally unaccompanied, except after a long time-lag, by an adequate provision of services and amenities. These, however, should be regarded as forming part of the indispensable equipment of every centre of economic activity; and their absence is just as much a sign of structural maladjustment as the lack of houses for the workers or a deficiency in facilities for transport. It should be regarded as part of the State's function to ensure that these services and amenities are available, either by providing them itself or, in suitable cases, by aiding other agencies to bring them into being.

(g)

to regulate the rate of contraction in industries which are suffering from an unavoidable diminution of the demand for their products, in such a way as to limit the amount of contraction by cutting out waste and thus reducing costs.

It may seem, at first sight, strange to include provision for the contraction of industries among the means of *increasing* employment. It is not really at all strange. Contraction will need to be less if efficiency can be improved by cutting out every form of waste and ensuring that the industries affected are run on thoroughly up-to-date lines. This is often nearly impossible to bring about in the absence of State intervention. Declining industries are usually unattractive to investors, and are often in difficulty for working capital—let alone for the additional capital they need in order to bring their methods up to date. The investor is apt to fight shy of them precisely because they are in difficulties, and because he is afraid of his money being used to bolster up the value of other people's capital already sunk in them, rather than to yield an adequate return to himself. These fears are often fully justified, from the standpoint of the private investor, even when the consequent lack of investment is not economically justified from the standpoint of the public. In default of the means of improving its efficiency, the industry continues to stagger along in a state of inefficiency which either causes it to lose more trade than it need, or allows it to hold its remaining markets only by cutting wages to a socially undesirable extent. Clearly the right course in such cases is for the State to come to the rescue of the declining industry, supplying the capital needed for reorganisation, but doing so only on condition that the necessary measures of re-equipment and improved business organisation are fully applied. The case is closely analogous to that already discussed under head (*a*). Indeed, the two cases may be the same, and the same alternative methods of handling the situation, by establishing either a Public Corporation or a Control Board, are available. The sort of instance I have in mind is shipbuilding, in which contraction ought to have been brought about not by a private combine intent on establishing monopoly, but under public auspices and under proper public direction as to the policy to be pursued.

When a condition of 'full employment' has been reached and, over industry as a whole, the demand for labour is threatening to outrun the supply, orderly contraction of industries acquires a different character; for it then becomes necessary to ensure that no industry shall make use of more labour than it really needs. Such a situation is of course analogous to that which arises in time of war, except that no such unlimited pressure on the supply of labour as arises under war conditions is likely to develop in peace-time. In peace-time, the aim of the whole economy is to satisfy as fully as possible the consumers' wants and needs, present and prospective, within the limits set by the available resources and the demands of leisure. There is no such attempt to get a quart out of a pint pot as must be made in wartime in order to squeeze out of the less indispensable occupations the last drop of labour that can be spared. There can, however, arise a situation in which the demands of industry generally for labour are so high that it becomes a matter of the first importance to prevent the absorption of undue amounts of it by any particular industry or service; and, in order to ensure the right balance, it may be necessary to take special steps to insist on industries which use labour in large quantities resorting to more mechanised and labour-saving methods of production. Inertia and trade conservatism may prevent this from coming about automatically as the general demand for labour rises; and in such cases the State may have to insist on a contraction of the labour supply even when the demand for the industry's products is actually expanding. The economically right degree of mechanisation in an industry depends on the relative scarcity of the factors of production, which can be employed in varying proportions according to the technical methods used; and it can by no means be taken for granted that the right composition of the factors will be achieved without any sort of compulsion being applied.

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to establish State productive agencies, in industries carried on mainly by private firms, in order to furnish a check on private costs or monopolistic practices.

The expansion of production in one industry may easily be checked by the existence of unduly high costs at the margin, or of monopolistic regulation of output or prices, not in the industry in question, but in some other industry which is closely related to it. The most obvious example is housing. The cost of houses can be seriously swollen by the existence of price rings, or of inefficiency at the margin, in the industries which supply essential builders' requisites and materials. After the last war, the development of public housing was rendered prodigiously expensive, and the Addison housing scheme shipwrecked, largely by the very high prices charged for building materials, including light castings, plumbing materials and, in effect, almost everything used in cottage construction. This happened because the industries supplying these products, being called upon to expand rapidly, experienced, even in the absence of organised monopolies, a sharp increase in the costs of production at the margin—that is, in the costs involved in producing the last of the additional units that were required. The existence of a certain demand, dictated by public housing policy, enabled all firms whose costs were below those of the least efficient firms to charge prices which yielded a satisfying profit to these firms, and therefore a large surplus to the efficient. Yet there was a slowness in expanding output capacity by the creation of new, efficient factories. This was partly because the existing situation suited very well the more progressive firms already in the trade, from which the expansion of capacity could most easily have come, partly because of deliberate restrictions on the entry of new firms imposed by means of rings of the existing firms, and partly because of sheer inertia among potential competitors or uncertainty about the continuance of the boom conditions or fear that regulative legislation for the control of prices might be introduced.

It would have been highly advantageous if at that time the State had been ready to enter the field with factories of its own, for the purpose not of driving out the existing firms, except those which were below a reasonable level of efficiency, but of keeping them up to scratch and preventing them from charging excessive prices. The opportunity for doing this was there, in that there were available disused war factories which could readily have been turned over to the manufacture of builders' supplies; but it was not taken, doubtless because the vested interests, and the prejudices against State manufactures in time of peace, were too strong. This same situation and the same opportunity will recur after the present war.

In the sphere of armament-making, the State has for a long time past purported to follow a policy designed to keep down private costs and prices by maintaining publicly owned productive establishments as a check on private costs. Woolwich Arsenal and the Admiralty Royal Dockyards have been supposed to serve this purpose, but have in fact done so only to a very small extent. How far the failure to use them in this way has been deliberate, it would take too long to argue; but it is undeniable that they have too often been allowed to lag behind in productive equipment, and have not been equipped to compete effectively with the private contractors over more than a narrow range of work. Most naval shipbuilding has deliberately been done in private yards, rather than in those belonging to the State; and Woolwich Arsenal was quite deliberately cut down to a skeleton staff after the last war, instead of being allowed to engage in civilian work in order to keep its plant fully in use and thoroughly up to date. These facts will, of course, be quoted as showing the inherent inefficiency of public enterprise. What they do show is that public enterprise is inefficient when it is run by a Government and a Civil Service which intend it to be inefficient, for fear of rousing the antagonism of private capitalists by competing successfully with them. That industries run by politicians and Civil Servants are likely to be inefficient I think hardly anyone will deny. It by no means follows that public enterprises run by Public Corporations officered by men of business training and ability and given a sufficient autonomy from civil service control need share the same fate. Is the Central Electricity Board or the London Passenger Transport Board more inefficient than the coal industry, or even than I.C.I.? I venture to say that they are not.

This brings me back to the point that there is much to be said for turning a number of the great war factories after the war into State factories for the *competitive* production of a wide range of ordinary civilian supplies. This case is strongest wherever these factories can be economically converted to the production of goods of which private supplies are in the hands of any sort of monopoly or price-fixing association. It has been one of the greatest achievements of the consumers' Co-operatives in Scandinavia to embark on such forms of production—for example, cash-registers and electric light bulbs, both instances in which their competition successfully broke powerful private monopolist rings. I wish the English Co-operative Movement would use some part of its vast financial resources for this purpose (the Scottish Co-operative Wholesale Society has done so, to a certain extent, in the case of electric bulbs). But, especially under the conditions which will exist after the war, when the State will have many great disused factories on its hands, the thing could obviously be done much more easily and on a far larger scale by State than by Co-operative action.

There is a further reason for regarding this type of development as highly desirable for the purpose of cheapening production and enabling the consumers' needs to be quickly met in the coming period of post-war shortage. These State factories could be put to excellent use in making and popularising simplified 'utility' products, not of course according to wartime 'austerity' standards, but in such a way as to meet all reasonable requirements at minimum cost by eliminating unnecessary variations and bringing selling as well as manufacturing expenses down to a lower level. This, again, would of course be opposed ferociously by the advocates of private enterprise all along the line; but there is little doubt that the room for reducing costs by removing the expenses of 'monopolistic competition', as well as the excessive charges of monopoly, is very considerable, above all in the field of semi-luxuries, where an absurd profusion of unstandardised varieties and styles has hitherto been suffered to flourish unchecked.

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to make special provision for employing the labour of partially disabled or incapacitated persons, where such persons are most likely to be useful if they are employed under special conditions.

The employment of partially disabled persons may, if there have been heavy casualties, be a very serious problem after the war; and, in view of the changing age composition of the working population, there will also be special problems involved in providing suitable forms of employment for certain classes of elderly people, who cannot stand the intense strain of much modern factory work. It is no doubt better, where it can be done, to employ partially disabled or incapacitated people in ordinary factories, side by side with those who do not share their disabilities. But this cannot always be done; and there are special cases, notably among the blind, the tuberculous, and the seriously disabled, for whom separate provision is clearly needed. Work of this sort has been pioneered in the main by private agencies, with results which have been on the whole excellent as far as they have gone, but have been seriously restricted by lack of means. Workshops for the Blind and Papworth Industries are well-known examples. Quite apart from the war, the need for special provision of these kinds greatly exceeds the supply. Both such work, and the parallel provision needed for ex-service men, ought clearly to be undertaken by the State, either directly or in some cases in conjunction with appropriate voluntary social service agencies.

It may be argued that it would be better to pension off many of these people, rather than provide special means of setting them to work. But such a view is wrong, whether the matter is looked at from the standpoint of the individuals concerned or of the whole community. The partially disabled man or woman is happier and better off if he or she feels a sense of being useful than if conscious of being a burden; and the community will be short of labour after the war, if its affairs are managed with even rudimentary common sense. In particular, in trades where intensive mechanisation is leading to a pace or tempo of work which older people trained in different methods are unable to endure, it will be well worth while to explore the possibility of keeping factories to be manned mainly by such persons, where necessary with the aid of subsidies to bridge the gap between their costs and those of more mechanised establishments. The fact that such factories might need to be subsidised does not mean that, from the standpoint of the community, they would necessarily be conducted at a loss. The workers in them, if they were pensioned off, would have to be maintained at the public expense: if the loss per worker employed were less than the cost of the pension, the community would gain. In truth, quite apart from the money aspect, the community would be the gainer to the extent of the net product created by the services of the persons employed, their wages not being counted as a subtraction from the net product.

(j)

to establish special Public Corporations for carrying out large projects of development which are unlikely to be tackled effectively by existing agencies, either public or private.

The sort of thing I have here in mind is the building of a new industrial town, or the carrying through of a big scheme of land reclamation. There has been much discussion of the desirability of tackling our problems of urban congestion by decentralising a proportion of our urbanised industries into new towns. One great difficulty in the way of this is that there exists at present no type of body, public or private, that is in a good position for doing the job. The local authorities of the towns which are to lose populations are not likely to undertake it, except in the case of towns which are meant to be mere satellites, in their own near neighbourhood. County Councils, as they are to-day, are for the most part quite unsuitable, and would probably reject the chance if they were offered it—at any rate in the majority of areas. Regional authorities capable of undertaking such work do not at present exist: nor do they seem likely to come into existence in the near future. Letchworth and Welwyn, the existing places most nearly analogous to what is in view, were created by private enterprise, or rather by the efforts of private philanthropists and social reformers with very little help from the State. The efforts involved in bringing into being by this method over a whole generation two quite small townships were prodigious; and it seems most unlikely that they will be repeated. Only the State can take the effective responsibility for a policy of creating new towns; and the State, if it did undertake it, would clearly have to set up special agencies for the purpose.

The most natural way would be to establish, for each new town that it was planned to bring into being, a Public Corporation to own all the land, to make the town plan, to build or enter into contracts for the building of the houses, public buildings and other construction required, to grant loans to industrialists and traders for the establishment of factories, shops, inns, places of entertainment, and so on, and in short to act as both Estate Company and local authority for the new town during its foundation period. When it had been built and inhabited, the functions of local government in it could in due course be handed over to an elected Council, the Public Corporation remaining in being for the management of the collective estate. Such Public Corporations could not, of course, be absolutely independent. They would be subject to the supervision of a national co-ordinating authority; and they would have to work in close consultation with the existing County Councils and other authorities in the areas placed under their jurisdiction.

Somewhat similar methods might be adopted for the reclamation or development of areas suffering from economic backwardness, such as the Scottish Highlands and considerable parts of Wales. It should be an integral part of post-war employment policy not to leave such areas derelict; their dereliction is to be regarded as a part of the structural maladjustment from which the economy of Great Britain has been suffering for a long time past. Instead of a Grampian Power Bill we need a Highland Development Corporation with wide and far-reaching powers; and the needs of North and Central Wales for measures of development designed to raise their standards of living are no less than those of the Highlands and Islands. Nor are there wanting in England areas to which similar measures could profitably be applied.

In this connection, it is pertinent to draw attention to the enormous problem which will confront this country after the war if the general introduction of holidays with pay is really to mean what it is supposed to mean. If the tourist industry is left to adapt itself to the new situation without State pressure or control, it is easy to see what will happen. There will be a considerably extended provision of holiday accommodation and amenities for the better-off wage-earners, at prices which they alone can afford to pay; but very little will be done towards providing holiday-making facilities for those who are less well-off. In order to bring about this wider provision, it will be necessary for the State to play an active part, both by providing cheap holiday camps and centres on an extensive scale, and by preventing an inflation of prices in face of the shortage of ordinary accommodation which is certain to exist for some time after the war ends. This form of State action links up with the measures to be taken for the development of economically backward districts, many of which are admirably suited to become popular tourist centres during the summer months. Moreover, the universalisation of paid holidays is bound to mean a longer spreadover, so that the holiday trades will be less acutely seasonal than they have been hitherto. This will of itself tend to lower costs; but the reduction will not be passed on in lower prices unless special measures are taken to provide additional cheap accommodation and to check the exploitation of scarcity values.

CHAPTER VIII

COUNTER-CYCLICAL MEASURES AND MONETARY POLICY

THE MEASURES outlined in the preceding chapter were discussed from the standpoint of their usefulness in correcting structural maladjustments in the economic system, though the discussion inevitably lapped over at certain points into a consideration of cyclical unemployment as well. The purpose of the public works and other extensions of State activity in the economic field dealt with under the ten heads enumerated on page 95 was in each case specific, in the sense that it was that of fostering a particular kind of enterprise or employment, and not employment in general. We have now to turn to a discussion of those aspects of public policy which have to do with the prevention of cyclical as distinct from structural forms of underuse of resources. To the considerable extent to which cyclical fluctuations bear unequally on different trades and industries, the measures used in countering them may also have to take, where this is practicable, specific forms; but major attention will need to be directed to increasing the volume of activity and employment in general, rather than in any particular industry—except, of course, that the specific public works undertaken by the State, or at its instigation, with this object will need to be *useful* works, and not the equivalent of digging holes in the ground in order to fill them up again.

We have seen already that counter-cyclical public policy must be directed to two main objects—the stimulation of investment in capital goods and the prevention of wage-cutting policies which will result in a contraction of consumers' demand. To these two we may add a third—the prevention of monopoly practices which are designed to hold up prices either directly or by concerted restriction of output. Throughout, we must of course consider those aspects of monetary policy which affect either the level of investment in capital goods or the wage-policies pursued by businesses carried on for private profit.

Let us begin with the monetary aspects of the problem of investment. The process of making additions to the supply of money, in order to stimulate business activity, takes shape, under British conditions, mainly through the action of the Bank of England. The Bank has at its disposal two instruments whereby it can seek to add to the effective monetary supply. One of these is the lowering of 'Bank Rate', which is the rate at which the Bank is prepared to re-discount eligible bills of exchange. Directly, changes in this rate have little or no effect on the level of economic activity; and in practice no more re-discounting may be done at a lower, and no less at a higher, rate after a change. Bank Rate is important not in itself but as a signal displayed to the whole financial world—a signal indicating the opinion of the leading monetary authority about the trend of financial affairs. A rise in Bank Rate is taken everywhere as meaning that the Bank thinks money *ought* to cost more to borrow, a fall that it *ought* to cost less. Normally, the joint stock commercial banks and the City finance houses follow this lead, and change their own rates of interest for the types of loans they make in correspondence to changes in the Bank's re-discount rate. But there is no absolute compulsion on them to do this; and when, as occasionally happens, they do not, the phrase goes that Bank Rate is "ineffective".

The rates of interest which other banks usually move up or down in accordance with changes in Bank Rate are, like that rate itself, rates on money borrowed for short terms—discount rates charged on bills of exchange, rates charged on loans and overdrafts to customers, and so on. There is no similarly direct reaction from Bank Rate upon long-term rates of interest—that is, on the rates on long-term bonds or stocks. Changes in Bank Rate affect long-term interest rates only by a devious process, and quite often not at all. Medium-term rates—that is, rates on borrowings which lock up the money for a few years, as distinct from a few days or months, or from a long period of years—are much more directly influenced by changes in Bank Rate, because medium-term loans mostly come from the banks and finance houses which are the dispensers of short-term credit. Long-term investments, on the other hand, come under normal conditions largely from the savings of individuals or from the reserves built up by business firms or other institutions, including Insurance Companies. It is true that they come also from the banks themselves; but long-term investment by bankers is usually high when the demand for loans at shorter terms is low, and *vice versa*. The banks to a great extent treat long-term investment as a means of using funds which they cannot use in advances at shorter terms; and when foreign trade is stagnant, so that bills of exchange are scarce, and industry depressed, so that the demand for overdrafts is small, they turn over perforce to investments at longer term.

This very fact tends to make long-term rates of interest move to some extent in correspondence with short-term rates. In bad times, when short-term rates are low, the additional demand of the banks for bonds at long term raises their prices; and a higher price for a bond of £100 bearing *x* per cent interest means that the effective yield becomes lower. If this occurs in the case of existing bonds, there is bound to be an effect on the rates that can be charged on new loans; for any purchaser is free to buy either the old or the new. Thus, long-term rates are indirectly affected; but the process may take a considerable time, and there may be conflicting forces which prevent it from happening at all.

For example, in the early 'thirties, when short-term rates of interest were very low on account of the depression, long-term rates for a long time failed to respond. The reason for this was simple. During the last war, the British Government had borrowed, at one fell swoop, a sum of £2,000 millions at 5 per cent. The term of years for which this money was borrowed allowed the Government to repay it at par any time between 1929 and 1947; and no one knew when the Government would exercise this option. Consequently, there existed a vast sum of money yielding £5 a year for each £100 of nominal value, and liable to be repaid at any moment at par. £100 nominal of this stock could not, under these circumstances, be worth in the market either much less or much more than £100. No one would pay much more for it, for fear of being repaid at par; no one would sell it for much less, in expectation of being so repaid. Accordingly, anyone who could buy this stock could thereby get for the time being 5 per cent on his money; and, as long as this was so, no one was willing to accept much less than 5 per cent. If there had been only a small quantity of these 5 per cent bonds, they would soon have vanished off the market, and have ceased to have any effect. But there were too many of them for this to occur; and there were in addition other bonds possessing similar characteristics. The long-term rate was therefore held at or near 5 per cent at a period of abnormal depression, when 5 per cent was a highly deterrent rate for most potential borrowers.

Of course, this pegging of the long-term rate was not absolute. Persons who expected the Government to exercise speedily its option to repay, and expected repayment to be accompanied by a sharp fall in long-term rates, were ready to lend at once for less than 5 per cent, where by doing so they could get for a longish period the assurance of a rate above the level they expected to prevail after the Government had repaid the 5 per cent loan. Nevertheless, the long-term rate was held, until the Government did exercise its option in 1932, a good way above what it would otherwise have been, and was over this period quite out of its normal relation to rates on short-term borrowings. When the Government did act—long after it should have acted—one consequence was to give an enormous fillip to house-building, which, as we have seen earlier, is very greatly affected by the conditions on which money can be borrowed at long-term.

A depression of cyclical character usually carries with it a sharp fall in the demand for both short- and long-term borrowing on private account. There is less foreign trade; and this affects the demand for discounting of bills of exchange. There is less production; and this affects the demand for bank overdrafts. Indeed, the effect is usually more than proportionate to the fall in economic activity; for many firms which are doing a reduced business can meet their smaller needs for money out of their own reserves, without needing to borrow from the banks, or will prefer to sell their more liquid investments and use the money to finance their current business if the yield of these investments falls below the interest charged on bank overdrafts. At the same time, there is less investment—usually a great deal less—in new capital goods; and this diminishes the demand for long-term loans.

The remaining field of investment for loan money is Government borrowing, which can be either at long or at short term. Government short-term borrowing is done mainly by means of Treasury Bills, running for three months, which are competitive with commercial bills of exchange. Government long-term borrowing is done by the issue of long-dated bonds, bearing a fixed rate of interest, and usually repayable at par, at the Government's option, at any time over a period of years before the contractual date at which they must be repaid. Clearly, what will happen in the money markets in times of depression will be greatly affected by what the Government does. If the Government, smitten by the desire for 'economy', cuts down its borrowing, the demand for money will be still further reduced: if it increases its borrowing—for example, in order to finance an extensive programme of public works—its demand for money will help to offset the fall in the commercial demand. The effects will be different, at any rate initially, according as the Government borrows mainly in the short-term or in the long-term market; but we need not pause now to examine these differences, or to study the effects if the Government borrows also at medium term.

The essential point is that Government borrowing in a depression will, other things being equal, limit the fall in interest rates by providing an additional outlet for borrowable funds. But this, it will be objected, is surely just what ought not to happen; for the higher rates will discourage commercial borrowers, and thus make the depression worse. This argument has in fact often been put forward in support of a policy of public retrenchment in bad times. It is, however, invalid, for two reasons. In the first place, if the times are really bad, a fall in interest rates is likely to have very little effect on the volume of commercial borrowing; for no one will borrow if he expects a loss merely because the loss will be less when the rate of interest is low. The inducement to borrow is not a low rate of interest as such, but a prospect of profit over what must be paid in interest; and such a prospect is likely to present itself, on a sufficient scale, only when the depression is beginning to pass away. Secondly, it is not inevitable that the rates of interest should rise because the Government presents itself in the market as a borrower. They will do so, unless action is taken to prevent this; but it can be prevented, if the Government is prepared to take the necessary measures.

I shall come back to this latter point very soon; but let us leave it for the moment. If the Government borrows for the purpose of financing public works, the spending of the borrowed money is itself an addition to the demand for investment goods and causes an expansion in the demand for consumers' goods as soon as it is re-spent by those to whom it is paid over as wages, salaries, or other kinds of income. It thus helps to create the conditions of expanding demand required for a revival in the demand for money from commercial sources, which is the sign of increasing private economic activity. It does this most, and most effectively, if interest rates are kept low despite the Government's borrowing; for, as soon as the prospects of expanding demand appear, the levels of expected profit are affected by the interest that will have to be paid, and the extent to which private demand recovers is therefore also affected.

It was said at the beginning of this chapter that Bank Rate is one of the two instruments at the disposal of the Bank of England for influencing the level of economic activity. We have now seen that it is not a very effective instrument. The other banks can ignore a change in Bank Rate if it does not correspond to their own estimates of the financial situation—or rather they can for a time, and could altogether if Bank Rate were the Bank of England's only weapon, which it is not. Apart from this, whereas an increase in Bank Rate is usually something of a check on expansion—for there will usually be *some* borrowers who will be choked off by a higher rate of interest—a fall in Bank Rate may lead to practically no expansion in borrowing, if business men are in a pessimistic mood. Bank Rate is a much more powerful weapon when it is used as an instrument for stopping a boom than when it is used for stimulating a revival; but even for stopping a boom it is very often ineffective, because in a boom so many people are too optimistic to be choked off by a small rise in costs, and the Bank often hesitates to raise its rate to such a height as would be deterrent, because it cannot do this without stopping a great deal of fully legitimate business as well as the speculative over-optimism which it wishes to check.

The Bank of England has, however, a second weapon; and this has been in practice in recent times very much more important than the manipulation of Bank Rate. The Bank can increase or decrease the available supply of money by engaging in what are called 'open market operations'. These consist in the buying and selling of securities by the Bank of England in the open market. When the Bank sells securities, the purchasers have to pay it money; and it can thereupon annihilate this money, leaving a smaller supply thereafter in circulation in the hands of the public. When the Bank buys securities, this process is reversed. The purchase price is paid out to the public, which has thereafter more money to circulate from hand to hand. The Bank of England thus appears to be able to increase or decrease the supply of money at will, making money when it chooses and annihilating it again when it chooses. And so, within quite wide limits, it can—especially when exchanges rates are not pegged by the operation of the gold standard.

In fact, the consequences of the Bank of England's open market operations are immensely magnified through the instrumentality of the other banks. Money which is paid out by the Bank of England is commonly paid in by the recipients to their accounts in the commercial banks, which thus acquire, against debits to their customers, deposits in the Bank of England. Now, the commercial banks, in creating credits by making loans to their customers, follow a traditional practice of regulating the amount of credit they create roughly in accordance with their holdings of 'cash'. A ten to one ratio is customary, though in practice the thing is rather more complicated than this suggests, because the banks try to keep a balance between different sorts of loans, and not merely between cash and credit as a whole. This refinement, however, need not concern us here. What does concern us is that the commercial banks traditionally regard all deposits standing to their credit in the Bank of England as convertible immediately into cash, and therefore as equivalent to cash. Accordingly, they feel entitled to create about £10 of new credits for every £1 by which their deposits in the Bank of England are increased (and, of course, *vice versa* when these desposits fall). Thus a purchase of £*x* worth of securities by the Bank of England carries with it a tenfold expansion in the amount of credit of various kinds which the commercial banks by tradition feel themselves entitled to create.

Sales of securities by the Bank of England have the opposite effect of a magnified contraction in the basis of credit. Thus, we see that the amount of money which the commercial banks feel themselves entitled to put into active circulation is determined, traditionally, not by themselves, but by the Bank of England.

The amount of credit the commercial banks feel entitled to create, however, is one thing; the amount they actually do create is another. Banks cannot lend people money unless they want to borrow it; and, though they can always buy long-dated securities, things get no forrader if the sellers simply leave the purchase-price on deposit in the banks. Doubtless, if the banks were to step outside their appointed sphere, and were to start building factories with money created by themselves, something would happen; but British banks would be outraged at such a notion, and in any case persons as habitually cautious as bankers are in bad times are most unlikely to be ready to risk their money in new investments when regular business promoters are holding off. Thus it may happen that the commercial banks, on account of the Bank of England's policy, have plenty of lending power, but are faced with a lack of borrowers. When that does happen, the Bank of England's policy of easy money is ineffective: the additional money simply does not get created.

This is not pleasing to the commercial banks. Lending on overdraft is normally their most profitable line of business: they get no interest at all on their deposits with the Bank of England; and, even if the market value of their gilt-edged securities goes up, that is a poor consolation for lack of profits on current business. The bankers will lend if they can, up to the limit of the available supply of money, provided they do not deem the risks too great; and they will in fact to some extent lower their standards of credit-worthiness in bad times so as to grant advances for projects which they would reject without hesitation if business were brisker. But borrowers of any sort are scarce when the business outlook is gloomy, and the mere in-pouring of fresh money by the open market operations of the Central Bank is no infallible cure for a lack of confidence among business men. If their confidence is not seriously undermined—if they are merely a bit doubtful, and not really pessimistic in a settled way—an infusion of bank money will probably bring them round. But if depression has advanced far, it will be unlikely to work unless it is reinforced by other methods.

This amounts to saying that, when a business recession is small, and is due mainly to psychological rather than to objective causes, open market operations may do well enough to jerk things back into the straight course. When, however, there are objective causes, or the depression has been allowed to go far, other measures will be needed in addition. The State will have to come in as an investor, with public works, to take up the additional money which the banking system stands ready to provide and to put this money into active circulation. Once in circulation, it will go on circulating, unless the mood of the business world is very black, as it was in the United States in the early 'thirties. If the mood is black, there is nothing for it but further action by the State, until as a consequence of the plenty of money the prospects of profit from increased production become too attractive for even sulky business men to resist them. The sulkier the business world is, the more money the State will have to spend into circulation. It can bring them round in the end, provided only that it sets no limits to what it is prepared to do.

This, it will be seen, emphasises the importance of the State acting promptly, before recession in the business world has gone far. The sooner the State acts, the less will it need to do in order to get matters right.

All this relates, of course, solely to cyclical conditions, and not to any tendency there may be towards underinvestment *in good times.* This chapter is about the methods of preventing cyclical unemployment: the methods of combating endemic unemployment are discussed elsewhere in this book.

I have spoken so far as if additional bank money could come into effective existence only by a double process—the enlargement of the 'cash basis' by the Central Bank, and the creation on this basis of additional credits by the commercial banks. This is not quite true. The Central Bank can itself push money into circulation by investing in capital goods; or the Government can borrow money directly from the Central Bank and spend it on anything it pleases. The Bank of England has in fact pursued this course to a certain extent by creating subsidiaries for investment purposes and by advancing considerable sums to industries in need of reorganisation or recapitalisation; and it may be added that the commercial banks, through the Bankers' Industrial Development Company and other similar agencies, have acted in a like way. This sort of action, however, which has been largely done under Government inspiration when it has been done at all, has been on a relatively small scale; and the Government has favoured it rather in order to escape pressure to invest itself than out of any real belief in the policy. In the event, it has been done much too timidly to produce any appreciable results. Nor has the Government in time of peace borrowed directly from the Bank of England on any considerable scale. There is an ancient prejudice, dating from the Napoleonic Wars, against such Government borrowing, which is supposed traditionally to be a sign of spendthrift finance. The Government, when it borrows, usually prefers to have recourse to the ordinary markets for long or short loans. This is deemed more respectable by orthodox financiers; and it can be pretended that what is being borrowed is 'real' money, and not money newly created in response to the Government's demand for it. This is pretended even when the commercial banks in fact create the money and lend it to the purchasers of the Government's loans, and even when the banks themselves buy the loans with money which, aided by the Bank of England, they have themselves created out of nothing. It is still deemed somewhat ungentlemanly to mention to an orthodox banker the obvious fact that he habitually creates and destroys money: such men still prefer to think of themselves as merely transferring money which somehow exists independently of their wills. This, however, is all mumbo jumbo. If the Government, or anybody else, borrows money from the bankers so as to increase the total amount in circulation, there is not the smallest doubt that this money is created by the banks—or that an opposite act of money-destruction is performed by them when the supply of money in circulation is reduced.

The question may fairly be asked, Why should the Government, if it wishes to increase the amount of money, borrow it from any bank, and pay interest on it when the bank has created it, instead of creating the additional money itself, without incurring any charge for interest? Why indeed? Yet the alternative process is not quite so simple as it sounds; for, in order to do this, the Government would have either to issue all the additional money it needed in the form of currency or to set up a sort of banking business on its own. Under modern conditions most money consists not of cash or currency notes but of entries in bankers' books. The amount of coins and notes issued to the public is simply the amount needed for settling such transactions as people do settle in cash and not by cheque—that is, principally, wage-payments and small retail purchases—and for supplying as much in addition as people actually choose to keep about them for current use, or the commercial banks to hold in their tills and safes as a reserve against their customers' calls for cash. The demand for cash, being largely based on wage-payments, depends principally on the levels of wages and employment: the supply of cash responds to the demand, and plays no important causal role. The important thing is the supply, not of cash, but of bank-money—of central bank money in particular.

If, then, the State were to meet its expenditure on counter-cyclical measures by printing as many notes as it needed and paying all its bills in these notes, there would be an enormous unwanted addition to the supply of cash, and most of these notes would promptly be paid into the banks and not paid out again. The effect would be a great enlargement of the cash basis on which the banks, if they followed their traditional practice, would be entitled to create credits, and there would be a strong pressure on the banks to do this, because the notes would yield them no interest. The acquisition of the notes, however, would not give the banking system as a whole any greater effective power to create credits than it would have possessed without them. What would happen would be that there would be the less need, or perhaps no need at all, for the Bank of England to engage in open market operations in order to enlarge the supply of money available for lending out from the commercial banks. The Central Bank would be the poorer to the extent of the Government's usurpation of its traditional function of making a profit out of the issue of its notes, and further to the extent to which the Government's notes resulted in a restriction in its creation of deposits by means of open market operations. The commercial banks would suffer no disadvantage unless the Government note-issue, added to the issues and deposits of the Central Bank (which latter, as we have seen, the commercial banks traditionally treat as 'cash'), were so large as to compel them to hold a higher proportion of their total assets in non-earning 'cash' and a smaller proportion in interest-bearing loans and securities. The Government, on the other hand, would be better off by the amount saved in interest charges. Whether the Government would get its public works free of principal as well as of interest costs would depend on whether the notes were left permanently in circulation or were subsequently redeemed.

If the notes were left permanently in circulation, the cash basis would be permanently enlarged by them and the power of the banking system to create credit would be correspondingly increased unless banking practices were modified. This would tend to raise prices in an inflationary way, unless the banks altered their ratios of credit to cash so as to leave in the aggregate no more money than would have come into existence in the absence of the Government notes. The banks, however, would lose heavily by doing this; for they would have to carry a smaller proportion of earning to non-earning assets. They would therefore not do it if they could help it; and if they were forced to do it they might be unable to cover their costs without raising their charges to their customers, and thus making money dearer to borrow—if even so. In effect, what happened during the last war, when the Government issued Treasury Notes, was that the cash basis was enlarged in the way described, and the credit superstructure with it, so that prices rose faster than they would otherwise have done.

What would happen if the Government, instead of printing notes to cover the whole of its bills for public works, went into the banking business, and created credits for itself? It could not do this merely by setting up an ordinary commercial bank, related to the Bank of England in the same way as the other commercial banks. For, in order to create credit as a commercial bank, it would have to have a cash basis, either in cash or bullion or in the form of a deposit balance at the Bank of England, and its power to create credit would be limited by the size of the cash basis and by the policy of the Bank of England in determining the size of the cash basis as a whole. If it created credit faster than other banks within the system, the recipients of cheques drawn upon it would be continually paying them into other banks, which would then, in the Bank Clearing, demand payment from the Government Bank in the form of a transfer to themselves of parts of its balance at the Bank of England. This balance would soon be exhausted, and the cash basis on which the Government Bank could create credit would vanish as soon as it had exhausted its stocks of coin and bullion as well. Government Banks, when they operate side by side with ordinary commercial banks, and accept the ordinary banking rules, are subject to much the same limitations on their power to create credit. It is the Central Bank that settles how much credit is to be created: not the commercial banks, which must keep in step with one another, within the limits set to the total supply of money by the Central Bank.

But why should not the Government set itself up as a Central Bank, side by side with the Bank of England and with a power of money-creation independent of the Bank of England? If it did, it would indeed be able to create credit freely, on a cash basis similarly created by itself. But there would then be two Central Banks, to both of which the commercial banks would have to be related in the same way. If the two followed an agreed policy, and acted in effect as a single bank, jointly determining the supply of money, the system could work. Rome had two consuls, and Sparta two kings. But if they were to disagree, the system would be bound to break down, unless one could coerce the other. It would be evidently very much simpler, if the Government wished to enter into banking, for it to take over the Bank of England and thus acquire the power of creating money which the Bank of England has.

Would this enable the Government to finance its expenditure without cost? That it would, is a highly attractive idea; for if this were so, there would clearly be no more need for taxes. The Government would simply create such money as it needed, including the money required for meeting the Bank's expenses; and no one would be a penny the worse off. This is surely much too good to be true.

What stands in the way? The simple fact that goods and services cannot be had for nothing. They cost effort to produce: they use up productive resources; and the real costs of producing them have to be met. Under the existing economic system, the costs of production, after the elements of duplication due to successive stages of production and the changing hands of goods in intermediate stages have been eliminated, are the incomes of the producers, of the owners of capital resources, and of those who have recognised claims to a share in the product of industry. The incomes generated in the course of production balance the costs, including profits on both sides of the account. If the State claims the right to purchase a part of the product with money created out of nothing, there will be the fewer goods and services left to be purchased with the incomes generated in the course of production. A + B will be available to purchase A only. If, in these circumstances, the supply of goods and services remains unaffected by the creation of the additional money, either prices must rise till the whole of the money not used by the Government is required to purchase the remaining goods and services, or people will be left with money in their possession but no goods to be bought with it. In the one way or the other, a part of their purchasing power will have been cancelled, up to the amount represented by the goods and services acquired by the Government and paid for with the new money created by it.

But, it will be answered, this argument contains the unwarrantable assumption that the creation of the new money will not bring about any alteration in the total supply of goods and services, whereas if the Government spends it on creating additional employment it will. True. To the extent to which the Government's action, either in creating the money or in using it to get additional goods produced, does in fact add to the supply of goods and services, the Government can pay for these goods and services with the new money without depreciating the value of the money already in existence—provided it is in a position to prevent the banking system from using the increase in employment as a reason for creating yet more money beyond what is needed to exchange any increased supply of goods and services over and above those which the Government itself buys. It can do this up to the point at which a condition of 'full employment' is reached, so that no further emission of money can cause a further increase in the rate of flow of new goods and services out of the productive machine. At this point, however, it must stop; and thereafter it must either pay like anyone else for whatever it requires, or reduce the incomes of private persons by an amount equal to its own spending. It can do this either by taxation levied on the public in the ways to which we are accustomed or, at any rate in a Socialist community, by distributing to private persons only the amounts of income which it can afford to let them spend after its own calls on the productive system have been met—that is, in effect, by a different method of taxation levied directly upon industry and not on private persons. What the State cannot do, without bringing about an inflationary situation, is to go on creating money and buying what it wants with it after a condition of 'full employment' has been reached.

I have heard it argued that, if the banks can go on continually creating money out of nothing, the State ought to be able to do so too. But the condition on which the banks can create money is that they are also prepared to annihilate it. Bankers' credits are not gifts, but repayable loans. The banker does not claim to own the goods which are made with the aid of the money he lends: his claim is only to the interest he receives on the loan until it is repaid. There is nothing to prevent the State from entering into the banking business, either by taking over the banks or by superseding them or by competing with them, and doing exactly what they do. But this will not enable the State to own for nothing the goods which are made with the money which in its capacity as banker it creates. Beyond the point at which 'full employment' has been reached, the State as banker will need, just as much as the private banker does, to recover and cancel the credits it has issued before it can issue any more without inflationary effects. This is obvious as soon as one thinks it over. Money once issued does not finish its career in a single act of circulation. It is of value to those who receive it only because they can use it again, and so on, in an endless series, unless it is recovered and cancelled by someone who does *not* use it over again. Consequently, if the State went on issuing new money continually to pay for what it needed, beyond the limit set by the requirements of 'full employment', the amount of money in circulation would be continually increasing without any relation to the current increase in productive capacity, and conditions would become more and more inflationary with every fresh issue.

To say this is not to deny that the State, or the banks, can make additions to the supply of money without inflationary consequences, not merely once and for all, in the process of raising the economy to a state of 'full employment', but also thereafter to the extent to which additional supplies of money are needed in order to keep 'full employment' in being—in other words, in accordance with further increases in the resources that become available for employment. Indeed, the State, or the banks, can go further than this in a community in which productivity is rising, even if there is no addition to the number of the employed population. It is optional for a community to reap the benefit of advancing productivity either in lower prices or in higher money incomes accompanied by a stable price level. There are advantages and disadvantages in both courses; but I do not propose to discuss them here. My immediate point is that the State or the banks *can* create money without limit, but that they cannot go beyond the supply of money which is necessary for the maintenance of 'full employment' at the existing price-levels without causing an inflationary situation to develop.

This is as true of the banks to-day as it would be of the State if the State took over their functions, subject only to the fact that

States impose by law on the banking system certain restrictions on the right to create money, with the object of checking inflationary tendencies on its part. These laws are by no means always effective in preventing credit inflation; but they do keep it in check. Moreover, bankers themselves are in normal times usually so frightened of inflation that, except occasionally when they lose their heads, they are likely to make much more sparing use of their money-creating powers than the law allows.

What we must not do is to push the above criticism of the monetary 'cranks' too far. The visions of a millennium in which money can be created *ad lib* and used to buy goods and services without any adverse reactions on the purchasing power of those persons who are not allowed to make money out of nothing are absurd. But hardly less absurd is the dogmatism that denies the possibility of creating *any* additional money without inflationary effects. This latter view rests on an unspoken assumption that all the available productive resources are already being fully employed; and, except on this assumption, it is not true. But it is true that the State, if it wants within these limits to create money and use it for financing its own 'counter-cyclical' measures, must take over the Central Bank.

How much difference would it make in practice, from this point of view, if the State were to take over the Bank of England? Many people, especially among those connected with the Bank itself, argue that it would make very little. The Bank, they say, is already in effect controlled by the Treasury, and does what the Treasury tells it. It is not a profit-seeking institution, in the sense of determining its policy with a view to making as much profit as it can. It pays in fact a stabilised dividend, which it can cover without difficulty; and the requirements of its shareholders for profits do not in fact influence its policy. It does, in consultation with the Treasury, what it believes to be in the best interests of the British economy as a whole.

There is in this view a large element of truth—largest in time of war. Under war conditions, the Bank of England is in effect an instrument of the Treasury, doing what the Treasury tell it to do. But how far is this the case in time of peace? The answer, I think, is much the same as the answer to a parallel question about the House of Lords. As long as a 'sound' capitalist Government is in power, the Treasury and the Bank are not likely to disagree except on minor points. It may sometimes be difficult to know whether the Treasury is controlling the Bank's policy, or the Bank the Treasury's; but on most matters their policies will be the same. The situation is different when there is a Government which the Bank directors, or most of them, dislike; for then there is the possibility of a clash such as arose in 1931, when the Bank in effect held a pistol at the Government's head, insisted on deflationary measures at the onset of the world slump, in order to preserve the gold standard, and then, when its action had caused the fall of the Government, promptly collaborated with the new Government, which it liked better, in abandoning the gold standard only a week or two later. In the same way, the House of Lords does nothing while a Conservative Government is in power, but soon turns nasty if the complexion of the Government is changed.

This is not in any way surprising. The directorate of the Bank of England used to be almost wholly, and is still largely, representative of the opinions of high capitalist finance. It has latterly taken a number of industrialists, and Lord Keynes, into its inner councils; but it is much to be doubted whether it has really changed its spots. It could still make itself very awkward, in peace time, to a Government intent on pursuing a 'full employment' policy by methods distasteful to high finance and big business. Such a Government would be wise to begin by taking it over, and thus ensuring its compliance with governmental policies.

The commercial banks stand on a different footing. A Government in control of the Central Bank could create all the money it wanted in order to finance 'full employment' without taking over the rest of the banks—of course, using the Central Bank as an ordinary commercial bank for its own purposes or creating a subsidiary commercial bank of its own side by side with the privately owned banks. But these other banks, if they were hostile to the Government's policy, could even so make it very difficult for the Government to get its additional money into effective circulation. They could 'lose confidence', and refuse to make advances to the businesses which would need to expand their activities in order that a state of 'full employment' should be reached. They could, in effect, go on strike, just as other sections of big business can go on strike against a Government they dislike. The Government could to some extent counter this attitude by making advances through its own bank; but in order to do this on a sufficient scale it would have practically to supersede the existing banks. It may be held that the threat of such supersession would be enough to keep the commercial banks in order; and this would be true if the Government were firm enough in its policy and secure enough in its hold on power. But, if it were timid or shaky, the commercial banks might quite easily stand out against it, and be powerful enough to thwart its plans and thus discredit it. If they could prevent it from reaching a position of 'full employment', they could get their friends to turn on it and denounce it for its failure to cure unemployment, and so perhaps bring it down. A Government bent on carrying through a 'full employment' policy would be wise, as speedily as it could, to take over control of the main commercial banks as well as of the Central Bank.

The upshot of this discussion can now be briefly summarised. 1. The mere emission of additional money is not by itself a sufficient assurance that the money will be put effectively into active circulation. 2. A low rate of interest, or rather a system of low rates for loans of various kinds, is not by itself an assurance that investment will significantly increase. 3. An emission of money, accompanied by a parallel increase in Government spending on public works, can be relied upon to bring about an expansion of activity and employment, if it is carried far enough. But it may have to be carried a very long way if the business world is either hostile to the Government or in a state of acute pessimism about the prospects of profit. In such circumstances, a half-hearted policy may be useless; for the business world can up to a point counter Government investment by lowering its own willingness to invest. There is, however, a point beyond which the business world cannot stand out against courageous and persistent Government action. 4. The Government will be in the best position to take this action, and to defeat opposition, if it effectively controls the banking system. 5. The Government cannot, by taking into its own hands the right to create money, command a supply of goods and services *ad lib* free of cost; but it can, up to the point to which an additional supply of money is needed to finance 'full employment', create this money at no cost beyond the costs of management of its circulation. 6. Money itself can create nothing: it can merely lubricate, or fail to lubricate, the wheels of production and exchange.

CHAPTER IX

MONOPOLY AND COMPETITION

IN THE two preceding chapters, we have considered certain methods whereby the State can attempt to deal with unemployment in two of its most serious forms—structural unemployment arising from maladjustments of the economy in relation to contemporary developments of technique and changes in demand; and cyclical unemployment, the ebb of total economic activity which afflicts most the industries producing capital goods. We have now to consider a third kind of unemployment, or perhaps we should call it rather a factor tending to aggravate unemployment under all circumstances and of both kinds. Some mention has already been made of this factor in earlier chapters; but the time has now come to consider its influence in a more general way.

This factor is monopoly, including what is called 'monopolistic competition'. Monopoly proper, as we have seen, tends in most cases to cause the monopolist to stop production and employment at lower levels than would prevail under fully competitive conditions, because the monopolist is in a position to select the level of output that, in view of the state of demand, seems to offer the prospect of the largest aggregate profit. This level is normally lower than would be achieved, in theory, under fully competitive conditions, because the monopolist, in fixing his output, has to take account of the effect of increasing production on the prices he can command for the earlier units of output, on condition that he puts no more on the market, whereas the business man who is working in a fully competitive market can treat the price he will get for his products as independent of the amount he produces. When there are many sellers in competition, no one of them, by varying his output, will appreciably affect market prices. It will therefore pay such sellers to continue production up to the point at which there is no surplus at all over marginal costs to be realised by the production of further supplies. This means that they will always go on producing at the current price until their marginal costs have fallen to the lowest level per unit. On the other hand, where there are few firms, or only one, in the market, or where most of the firms act together in pursuance of a common output policy, the factor governing the level of output will be, not marginal cost in relation to a price taken as settled, but that relation between the total price received for the entire output and the total cost which will yield the largest net surplus. This will mean a smaller output.

This is, no doubt, a highly theoretical way of stating the contrast; for in practice conditions of unlimited competition are met with only in a limited number of industries, and even in these the theoretical conditions of what the economists call 'pure' and 'perfect' competition are never fully satisfied. On the other side, for reasons which we have discussed already, pure monopoly is almost as rare as pure competition. In most industries, we get something between the two extremes, but with enough monopoly in it at some stage of production to have a substantial restrictive influence on supplies.

I am not forgetting that quite often one of the reasons for monopoly is that competition, of the sort that actually exists, may stand in the way of the use of the most efficient methods of production, by preventing standardisation of products, specialisation of plants to a narrow range of work with a view to the fullest use of mechanical devices, and the reduction of selling costs, especially where sales are to be made in distant markets. There are undoubted technical advantages in monopoly, in many lines of business, and undoubted disadvantages in many of the forms which competition actually takes. Economists in their theoretical treatment are accustomed to demonstrate that under conditions of unlimited competition all firms are bound to be of the *optimum* size and efficiency for production at the lowest cost, because those which are not will inevitably be driven out of business by the multiplication of those that are. This involves the limiting case of an industry for whose products there is only demand enough to occupy *one* factory of the *optimum* size,—a case in which unlimited competition must lead to monopoly as its logical result. Actual conditions of competition clearly differ greatly from these theoretical conditions; for the most competitive industries are full of firms which differ greatly in both size and efficiency. It therefore cannot be said that monopoly will always result in lower output than would be achieved in practice under competition. The truth may even lie the other way, where the economies attending upon large-scale production and specialisation are great and where the market for the products is highly elastic, so that small changes in output do not involve much change in selling prices. What can be said is that the monopolist will nearly always produce in good times less than he could produce at a profit, because he will nearly always be able to make a higher profit by stopping short, and that in bad times he will tend to contract output more than it would be contracted under competitive conditions, in an effort to avoid or to reduce loss.

In the case of what is called 'monopolistic competition', the situation is somewhat different. The monopolist in the ordinary sense uses his position of vantage for extracting a high level of profit from the consumers. The monopolistic competitor incurs additional costs, and forces similar costs upon his rivals, in an endeavour to differentiate his goods from theirs in the minds of potential buyers, and thus establish as far as he can a 'proprietary' monopoly. He does not necessarily reap an excess profit; but the higher costs incurred in trying to do so raise the prices of his goods and thus diminish their consumption. Accordingly, industries subject to 'monopolistic competition', as well as industries subject to ordinary monopoly, tend to employ less labour than could be employed in them if neither their costs nor their profits were artificially inflated.

The effect of both kinds of monopoly practice bears directly, of course, on the demand for the products of the industries affected by them, at the prices at which these products are offered for sale. People buy less of these products than they would buy if the prices were lower; but they also in the aggregate spend more on them, so as to have less income left for buying other things. This may not be true in every case. There may be some products of which people buy just as much at a higher as at a lower price, at any rate over a fairly wide range of prices (salt, for example, or anything else that costs so little as not to matter); and there may be cases in which people spend less in the aggregate on a thing as its price rises because they can resort to substitutes or find preferable alternative ways of spending their money. Even in such cases it may pay to keep the price high, because the profit on each unit is so much greater at the lower level of output. (To this category belong certain luxury goods, such a refrigerators, and, or at any rate so the milk produeers seem to believe, milk). In general, however, the total sum spent on a thing will increase as the price rises; and accordingly people who are not monopolists will have less money left to spend on other things.

This does not mean that there is less money to spend; for the monopolists have it instead of the other people. In the case of ordinary monopoly, it will go into profits, unless some of it is handed out in higher wages to the workers employed. If it goes in wages, it will be spent like other wages, and so no harm will be done, except that wages will be unfairly distributed between different groups of workers. But if it goes in profits, a large part of it will either be invested in capital goods, or 'saved up' and not spent at all. Investment is a highly fluctuating factor; and we have seen already what happens to 'saved up' money which does not fructify in real investment. Monopoly profit thus both increases the instability of the economic system, by withdrawing money from use in bad times, and aggravates the maldistribution of incomes, in addition to lowering the total level of production and employment.

In the case of monopolistic competition the case is different; for here what happens is that more labour than is really necessary is used up in production (including selling activities). There is not necessarily any surplus profit, and there may be no additional unemployment. What happens is that effort is wasted, and the community thus gets less real income than could be put at its disposal.

Monopoly, in the ordinary sense, lowers the demand for investment in the industries to which it applies. For if it produces less than could be produced, it also calls for less real investment in means of production. This may seem to be untrue where a monopoly is go-ahead in installing the latest capital instruments; but in such a case yet more of these instruments would be needed if production were unrestricted. Where it is restricted, more expensive capital instruments usually mean less direct employment of labour as their correlative. As long as monopoly exists seriously only in a few industries, its principal effects will be upon the level of production in the industries which it controls. But as soon as it becomes widespread, each monopoly reacts far beyond its immediate sphere of influence, causing other monopolists to behave more restrictively than they otherwise would, and lowering the level of consumers' demand over industry as a whole. Moreover, the widespread existence of monopoly generates a subtle change in the psychological outlook of the business world. It sets men of business 'enterprise' racking their brains for means of getting rich, not by producing more or more cheaply, but by manœuvring themselves into a position which will allow them to control the conditions of production and pricing. This does not apply to industries which are working under conditions of monopolistic competition; and it is easy to see the difference in the psychological outlook of, say, the producers of inexpensive motor-cars and the producers of the steel from which the cars are largely made.

If the restrictive monopolist attitude becomes common among business men, and especially among those who belong to the financial rather than to the technical section of the business world, it has quite disastrous consequences on investment policy. The mind of the monopolist always tends to pessimism about new capital expenditure designed to expand output; he is much more disposed to spend money on buying up plant which he regards as 'redundant', and putting it out of use. The new worlds which he sets out to conquer are worlds of financial and not of productive adventure. He is always weeding his garden, rather than planting things which he wants to see grow.

In the past, monopolists have been kept up to scratch to some extent by the fact that they had no monopoly in the world market, and often by the fear of foreign competition in their own. It is no small part of the case for Free Trade, under capitalist conditions, that it limits monopoly. But of late there has been a growth not only of tariffs, quotas, and other devices for the protection of home industries, but also of international cartels in many fields. Such cartels are terribly restrictive. Based essentially on the notion of a limited world market to be shared out, they aggravate every tendency towards limitation of output. They also minister to the spirit of pessimism, and often cause business men to limit output still more than they would if they were fully alive to their own long-run interests. Protectionism too, while it of course causes expansion in some of the protected industries, tends, by its adverse reactions on international trade, to make business men think more of stable production for a limited market than of the possibilities of expansion.

Indeed, what is wrong with present-day capitalism throughout the world is, above all else, that it has so largely ceased to think in terms of expansion, and come to think more and more in terms of restriction and monopoly, both at home and abroad. This is for capitalism a fatal disease of the spirit; for it has been the very essence of capitalism to stand for expansion. The only even plausible defence for the existing distribution of wealth in capitalist societies has been that it is necessary to provide for a high rate of real investment, with a view to continuous expansion of productive power, and that the capitalists are the people who know best how to direct this process of investment, and should therefore be allowed huge incomes, not to spend on themselves but to invest. As soon as they stop doing this, their large incomes become a curse, dragging down the level of consumption in the present, and not offering in requital any prospect of an increasing standard of living in the future. Monopoly capitalism and idle resources go together: they are the linked signs of the waning of the virility of the capitalist system. That system in its prime, ruthless as it was, did put the fruits of technical discovery to ever-increasing use. But to-day, for the most part, the key personages of capitalism seem mostly intent, not on conquering new fields of production, but on ploughing-in as much as they can of the present crop.

How can this disease of capitalism be checked, if indeed it can be checked at all? Pains and penalties can be tried, to check it in its grosser forms, where the case against it admits of legal demonstration. Excessive prices, beyond what can be defended on the score of costs, can be made illegal; and combines convicted of certain forms of 'restraint of trade' can be broken up. But the world has not, hitherto, made much of a success of these methods of discouraging the growth of monopoly practices; and of late years it has appeared to be turning its back on the attempt, though there is naturally a recrudescence of 'anti-profiteering' legislation in time of war. 'Price regulation' by law is not easy to apply to most types of finished goods; and though it can be applied to the more standardised types of manufactures and semi-manufactures, as well as to some primary products which can be conveniently graded or marked, there are difficulties even in these cases. As for the breaking-up of combines, it appears to have gone right out of fashion, and to have been replaced by a desire to promote them in the hope that they will not demean themselves too badly after all.

The greatest single reason why price-control has become discredited of late years as a means of coping with 'profiteering' is that it has so often been used for a quite opposite purpose—to maintain minimum or standard prices, rather than to fix maxima. In a world beset by the disorders of structural and cyclical unemployment, the problem often seems to be rather that of keeping prices up than that of holding them down. In agriculture, in coal-mining, and in the cotton industry, the aim of State intervention has been to prevent prices from sinking unduly low; and concern for the standards of living of the employed workers, as well as for the profits of the owners of capital, has suggested policies of artificial price-maintenance, which have received Trade Union as well as capitalist support. In steel, the dislocations into which the industry fell after the last war became an excuse not merely for special measures designed to restore it, but for the creation of a steel-makers' monopoly with almost unlimited power to exploit the home consumer. In all these instances, the State was far too much concerned about keeping the industry from going to ruin to have attention left for preventing it from using the help given it for the pursuit of monopolistic gains.

This situation could exist, over a wide range of industries, only because the economic system as a whole was in a bad way, and there was general unemployment of resources. In such a situation it was plausible to argue that, if the rot could be stopped in this or that particular industry, a valuable contribution would have been made towards recovery in the system generally. It could not be good to have firms going bankrupt right and left; and, if this could be prevented, surely everybody would feel the benefit. But in fact the engineering of recovery by this method, applied to those industries which had for one reason or another the strongest political pull, while it doubtless benefited those engaged in these industries, reacted unfavourably on the rest of the community, including the industries which did not get special privileges. Dearer steel was of advantage to the owners of shares in steelworks, to banks which had lent them money, and to the workers they employed, from managing directors down to labourers. But it was a disadvantage to the steel-using industries, except where they were themselves so organised as to exact similar privileges—and even then it would have suited them better to enjoy the privileges themselves, but to have them denied to the steel-makers. Whether or not the prices charged by industries which obtained from the State the right to make use of monopoly practices were too high absolutely, there can be no doubt that they were usually too high in relation to the prices which could be got by industries not similarly privileged.

In effect, depression became a screen behind which monopoly could develop, and so did structural maladjustment; and it came to be widely considered that where prices were in general too low for 'full employment' to be possible under profit-seeking conditions, it could not but be a good thing to push up some of the prices, even if nothing were done to push up the rest. The higher prices were not felt to be too high, because the lower prices were felt to be too low. The monopolist who could get himself into a position to choose an output below what he could have produced at a profit—but not at so high a profit—was not scrutinised, because the eye of the community was on the low prices it wanted to raise to a remunerative level, in the hope of stimulating employment, rather than on the high prices which it ought to have wanted to bring down, especially where they were for semi-manufactures entering into a wide range of finishing trades.

If there had been 'full employment', instead of widespread unemployment, it would have been impossible for anyone to think in this way. For then it would have been clearly apparent that monopoly was a means of defrauding the consumer of his due. If there had been fairly good employment, with most firms doing tolerably well and few bankruptcies in the offing, it would have been hardly less difficult to put this line of thought across; for the monopoly practices would have been clearly visible as reasons why the economy was stopping short of 'full employment'. Only general depression could so obscure men's vision as to make them solemnly argue that total employment could be increased by entrenching groups of monopolists in the key positions.

There is, no doubt, an exceptional case in which monopoly might have advantages, even from the standpoint of the economy as a whole—the case in which monopoly is not monopoly any more—the case of foreign trade which retains its competitive character. Monopolistic organisation of an industry might enable it to drive harder bargains in international trade, so as to shift the 'terms of trade' in favour of the country establishing such monopolies. In other words, monopolistic organisation on a national basis might increase the aggregate price obtained for exports, as well as the price per unit, and thus ease the foreign exchange position. But in practice, the establishment of a monopoly capable of achieving this result in respect of exports usually means conferring also the power to exploit the home market.

The State, then, has been prevented in recent years from attacking monopolies, and has even been led to encourage them in many cases, because of structural maladjustments in the economy and because of the general incidence of depression. It has wanted to encourage industrial revival by making production more profitable, and has therefore turned a blind eye to profiteering and to forms of monopoly capable of use for profiteering in the event of a recovery setting in. It has ignored the general for the particular case, and has fallen into the fallacy of assuming that what is good for one industry, or for a few, from the standpoint of those engaged in them, must be good for all, and for the whole people.

The right way to increase profitability for industry as a whole is not to help particular claimants to snatch more for themselves out of a limited pool, but to increase the size of the pool, and let everyone draw upon it. This is not meant to exclude special measures for the reorganisation of industries which have been allowed to get into a mess, but to suggest that such reorganisation will be well done only when it can be made to fit in to a general plan of economic expansion, and can, without endangering its own success, be accompanied by the imposition of proper safeguards against the abuse of the powers conferred in connection with it. As we have seen in the chapter dealing with structural maladjustments, industrial reorganisation is in many cases indispensable; but it must be reorganisation as part of a general plan for the achievement of plenty, and not an authorisation from the State to pursue scarcity and dearness as the means to restoring profitability. It should therefore be accompanied by public regulation, at least to the extent needed to prevent excessive charges, and to ensure continuous public pressure to keep costs as well as prices down. Such safeguards for the public can be insisted on much more easily when a condition of 'full employment', or something approaching it, can be taken for granted in the economy as a whole, because the State has accepted the responsibility for securing and maintaining it by every means in its power.

What has been said in this chapter must not, however, be construed as a plea for a return to fully competitive conditions. In many types of industry, in which the economies of large-scale production are high and the capital costs of establishing a technically efficient plant very great, fully competitive conditions cannot exist. The number of sellers is bound to be few, and the advantages to these few sellers of entering into common arrangements for the regulation of the market are bound to be great. Nor are these advantages by any means all of an anti-social kind. For example, agreements to observe standard specifications, to specialise plants to particular uses and not to duplicate the manufacture of varieties for which there is only a narrow market, to adopt joint sales arrangements in distant markets, to pool patents, and to engage in coordinated research, are all technically advantageous in themselves, and tend to a lowering of the costs of production. It would be foolish for the State to obstruct these tendencies, even if it could.

The emphasis, under modern productive conditions, must be put on the regulation of monopolistic tendencies rather than on their prevention. Where private monopoly seems certain to lead to anti-social practices, because the pursuit of profit plainly dictates restrictive policies—for example, where an increase of output is likely to mean a sharp reduction in prices without an equivalent fall in costs—regulation of monopoly practices will need to be drastic, and may need to be so drastic that there is no practicable way of enforcing it short of transferring the industry concerned to a Public Corporation, and thus getting rid of the profit motive altogether. Where the advantages of restrictive practices are less pronounced owing to more elastic market conditions and/or more favourable cost-conditions on the supply side, or where their advantages proceed largely from removable causes, such as the bad organisation of the industry or its structural maladjustment to changing market openings, a less drastic regulation may suffice; and the appropriate remedy may be not the establishment of a Public Corporation on a non-profit basis, but the establishment of a Control Board armed with wide powers. It is, of course, indispensable in such cases that the Control Board shall be so constituted as to express the will of the public, rather than of the industry regarded simply as a source of profit. Any such Board should have an executive Chairman drawn from outside the industry, or at any rate entirely without financial interest in its profitability, and should include other members chosen to represent the public's, rather than the industry's point of view. Moreover, the Board should not be allowed to exercise any compulsory powers over the industry without the explicit sanction of the Government, through the appropriate Minister in charge of the general policy of employment and economic development. The Board's Chairman should rank as a public servant (not a Civil Servant, in the ordinary sense) equally with the Chairmen of Public Corporations such as the Central Electricity Board; and the representatives of the industry itself upon the Board should be made to understand that they hold their offices in trust for the public, which is concerned that the industry shall be as prosperous and active as it can be made by legitimate means, without recourse to anti-social measures designed to increase its profitability at other industries', or at the consumers', expense.

This type of Industrial Board is worth trying out both in industries which are in urgent need of reorganisation and in other industries in which the advantages of concerted action are large, but do not take *mainly* the form of output restriction for the purpose of maintaining prices. It would be the logical accompaniment to such a policy of regulation of private enterprise, as an alternative to outright socialisation, to prohibit absolutely the practices of output or price regulation, or restriction on the equal trading opportunities of new firms or firms outside the ring, in any industry not regulated in this way. The only private monopolistic practices tolerated should be those endorsed by the Government in the public interest (i.e. on technical grounds) on the recommendation of a Public Industrial Board constituted on the basis here proposed. There should be an Economic Tribunal with wide powers to suppress and punish all attempts to adopt restrictive price or output policies except such as had received this public approval. Anti-cartel legislation would have some hope of success if a way were left open in which industries needing collective organisation and the establishment of common codes of business practice could get what they wanted, subject to the necessary safeguards for the public interest, by going about the matter in the approved way.

How many industries it would be desirable to regulate by means of Industrial Boards (and how many to transfer to Public Corporations) I do not pretend to say. Nor shall I attempt in this book to go into any detail about the working of the Boards, or the ground which any particular Board should cover. Where, as often occurs, monopoly is much more strongly entrenched in one part, stage or process of a diversified industry than in others, it would be fully practicable to establish a Board (or a Corporation) for that section alone, if that seemed the better way. It would be possible to experiment first with a few Boards, and to create more when experience had shown the best way of operating them; or Boards of somewhat different types could be set up for different types of industry. In all cases, however, it is essential to preserve intact the principle that the Board is to be regarded as a public body regulating the industry in the public interest (including that of the industry itself, to the extent to which the two are compatible). Accordingly, the executive power must be vested in the Chairman of the Board, or in the Chairman jointly with the other State-appointed, disinterested members; and the Chairman must be definitely a public servant without financial stake in the industry over whose fortunes he presides. These conditions are necessary in order to ensure the Boards' compliance with the requirements of an all-round 'full employment' policy and to prevent them from becoming agents of restrictive monopoly. If they fail in this, there will be no alternative to superseding them, and bringing the industries which they have failed to control in the public interest under the rule of Public Corporations.

CHAPTER X

'FULL EMPLOYMENT' IN ITS INTERNATIONAL ASPECTS

'FULL EMPLOYMENT' has been considered in this book, so far, purely as a national problem, that is, as a problem of getting all the productive resources of a single country into the fullest possible use, without any discussion of the reactions of such a policy on its economic relations with other countries. It is, however, plain that there would be such reactions, and that they would be of great importance in any country which normally depended to a considerable extent upon foreign trade. Great Britain, for example, imports a large proportion of its foodstuffs and of the raw materials used in its industries, and pays for these imports partly out of the interest and dividends received on the overseas investments owned by British residents and partly by its own exports, chiefly of manufactured goods and of coal and by the services of its shipping and its financial agencies.

Evidently, unless the structure of the British productive system were greatly changed, the establishment of a condition of 'full employment' would mean an increased demand for imports. Industries would need more materials, and the increased incomes accruing to consumers would involve an additional demand for foodstuffs from abroad. These additional requirements could be paid for only by larger exports, unless—which is most improbable—the 'terms of trade' were to turn in favour of Great Britain to a marked extent; that is, unless each unit of British goods exported could be exchanged for a larger quantity than before of imported products. It therefore appears that, in order to sustain a policy of 'full employment' in Great Britain, it would be necessary either to make a large addition to British exports, or to alter substantially the structure of the British economic system, in such a way as to reduce dependence on imports through higher home production of foodstuffs or of materials, or of both.

This is, indeed, a considerable understatement. Great Britain after the war will be faced with the necessity of largely increasing exports in order to be able to pay for the same quantity of imports as before the war—let alone an increased quantity. This necessity will arise because a large part, if not the whole, of the overseas income-yielding assets owned by British residents will have been sold in paying for war supplies, while others may have been lost through other causes—for example, if India and Burma and Malaya do not continue to make any payment to British investors. India, indeed, will very likely have liquidated its net indebtedness to Great Britain before the war ends; and there is no certainty that the flow of income to Great Britain from Burma and Malaya will be resumed. If over and above this change in Great Britain's creditor position in the world economy the 'terms of trade' change against Great Britain, on account of a rise in the prices of foodstuffs and other primary products in terms of manufactured goods, the increase in exports needed to pay for imports at the pre-war level will be larger still; and such a change in the 'terms of trade' is likely, if the countries producing primary products have a say in determining the conditions of post-war international exchange.

It will be difficult in any circumstances for Great Britain to export enough to pay for imports at the pre-war level; and this fact will be used as an argument against the attempt to establish a condition of 'full employment', on the ground that the additional imports required in connection with such a state of things cannot be afforded. It will be argued that Great Britain can have 'full employment' only if the British people is prepared to accept a lower standard of living which will keep imports down to a level which can be afforded and also expand sales of exports by cheapening production at home, or if, alternatively, Great Britain can so increase home production of foodstuffs and materials as to keep the demand for imports down to the level called for by British ability to pay with exports or with shipping or other services and with such net income from abroad as may still be left.

Let us make no mistake about it. This problem of paying for imports after the war is a real problem, and it will not be easy to solve it unless the post-war world is, economically, very different from the world that existed between the wars. It is not, however, a problem created by 'full employment', though 'full employment', by calling for a bigger quantity of imports than would be needed if the level of employment were lower, will mean that more goods will have to be exported in payment—unless indeed Great Britain increases its degree of self-sufficiency as employment expands. The problem of exporting enough to pay for necessary imports will exist whether Great Britain follows a policy of 'full employment' or not.

I do not propose here to discuss this wider problem at any length, because I have said what I have to say about it in a previous book, *Great Britain in the Post-war World*, and I must refer my readers to the arguments there advanced. The extent to which it will be possible for Great Britain to expand its exports after the war is partly a question of the prices at which they can be offered for sale—that is, of the technical efficiency of the export trades, their freedom from monopolistic restriction, the levels of wages paid in them, and the value set on British money in terms of the monies of foreign countries and of the countries of the British Empire. It is, however, quite as much a matter of the willingness and ability of other countries to buy imported goods—factors which, of course, depend largely on their ability to sell their own exports on satisfactory terms. Indeed, the extent to which other countries are willing and able to buy is likely to be the final determinant of the ability of Great Britain to sell and accordingly also of British ability to buy. This is not so much of a truism as it sounds. What I mean is that the final determinant of the level of British ability to sell, and therefore to buy, will be the level of economic activity maintained over the world as a whole and the degree of freedom maintained in exchanging goods and services across national frontiers. If world production and world trade are active, British export trade will be active too; for the incentive will be there to improve efficiency and to make short work of monopolies that stand in the way of its expansion. The British people will have to see to that, as the only way open to it of maintaining and improving its own standards of life.

Clearly, this condition of high activity and production over the world as a whole cannot be satisfied unless the world as a whole is following a policy of 'full employment'. Unless in each country, or at any rate in the main countries, there exists a determination to make the fullest possible use of the available productive resources, it will be made much more difficult for any one country to follow such a policy. It should be a term of the coming peace settlement—one of the most important of all—to pledge each participant to do its utmost to prevent unemployment within its own frontiers and to set on foot, internationally, such measures as will make it easy for this to be done.

Pray observe, I am not saying that the pursuit of a policy of 'full employment' in each leading country is a guarantee of a high level of international trade. It is a condition of it, but not a guarantee. For it is possible for some countries in a very high degree and for all in some degree to pursue the objective of 'full employment' along autarkic lines. Large countries especially, where they are in possession of a wide range of diversified economic resources, can aim at 'full employment' by making larger use of their own resources in producing for home consumption and thus achieving economic expansion without a corresponding growth in import and export trade. This is much harder for some countries than for others—perhaps hardest of all for Great Britain, among the greater States; but it is practicable everywhere, in some degree. It involves of course restrictions on imports, such as will effectively check their increase as internal purchasing power is increased by 'fuller employment'. Tariffs can contribute to this end; and, where they are not enough, they can be supplemented—or indeed replaced—by quotas, licensing systems, State monopolies of imports of particular kinds, and, finally, by restrictions on the supply of foreign exchange for the making of purchases abroad. Or, again, recourse can be had to subsidies which will enable home products to drive imports out of the market, or to total prohibitions upon imports of certain sorts.

The world had abundant experience between the wars of these autarkic devices for increasing the volume of employment within a country, or at all events for diminishing the volume of imports and the demand for foreign exchange, and for giving the home producers protection or even complete monopoly in the home market. The lesson of this experience was that such devices can be exceedingly effective in reducing the level of foreign trade, but that their effectiveness is much less in increasing the volume of home production. No doubt, the Nazis, with their autarkic methods, did succeed in reducing unemployment to a low level. But this result was achieved, not by *autarkie*, but by the other measures taken by the State to increase the level of investment, above all in all those industries which were essential to war preparation. The 'public works policy' created the employment: the *autarkie* did not create it, but was necessary to it to the extent to which the Germans were determined to concentrate the expansion of activity as far as possible upon the use of home resources, and to prevent it from leading to a rapid growth of imports. They considered, no doubt rightly, that, with the world as it was and as they were doing their best to make it, they would find it impossible to expand their exports at remunerative prices to an extent sufficient to meet the additional demand for imports which would have followed upon their expansionist policy in the absence of special restrictions. Over and above this, *autarkie* to the extent to which they carried it was valued by them as a means to achieving greater self-sufficiency in war. But that is another story. What matters at present is to realise that *autarkie* was not a cause of

German economic expansion, but a policy requisite in order to prevent such expansion from being fully reflected in the growth of imports.

A policy of 'full employment' can, then, be pursued along autarkic lines, with greater or less difficulty, according to the range of the home resources possessed by the country adopting it. Moreover, it may be impossible to pursue a policy of 'full employment' without some resort to autarkic methods if other countries are not prepared to expand their imports in such ways as will allow the country which is pursuing it to expand its exports fast enough to cover the purchase of the additional imports its citizens, with their enlarged incomes, would like to buy. Thus, if one country goes in for 'full employment' on largely autarkic lines, and another country refuses to accept 'full employment' as its object and resorts to deflation instead, a third country which wishes to pursue 'full employment' with as little resort to *autarkie* as possible will be driven to be much more autarkic than it wishes to be because the others refuse to buy more of its exports in return for exports of their own. The lower the level of world trade is, and the greater the obstacles put in the way of its expansion, the more autarkic each country that makes 'full employment' its objective will be driven to become. The countries which will fare worst under these conditions are those which will suffer the greatest economic disadvantages if they are driven to rely more on their own resources and less on exchanging what they can produce most easily and efficiently for goods which can be produced much more easily and efficiently abroad.

It would be possible for Great Britain to pursue a policy of 'full employment' even if other countries did not. But this would mean that Great Britain would have to produce at high cost a great many things which could be procured much more cheaply from abroad, if only they could be had in exchange for British exports of things which Great Britain is well equipped to produce. As British dependence on imported raw materials would be very difficult to reduce greatly, and as imports of manufactured goods had already been reduced before the war mainly to specialities which it would be difficult to replace by home products, this would mean, in the main, that Great Britain would have to produce at home a much higher proportion of the food it needs. Up to a point, I am strongly in favour of this, where there is a chance of production being put on reasonably economical lines, or where there is a very strong nutritional case for increased use of a particular kind of food (e.g. milk, fruit, vegetables). But it would evidently impoverish this country to be compelled to grow at home greatly increased quantities of foodstuffs which can be had much more cheaply from abroad as long as there are means of paying for them; and it would be sheer calamity if the conditions of international trade after the war were to force such a policy upon this country, either absolutely or as the only alternative to leaving a large proportion of the available labour resources unemployed.

All this is, of course, a question not of yes or no, but of how much. I can see little possibility of Great Britain being able for some time after the war to expand exports to such a point as to meet the cost of all the imports that would be in demand if no restrictions were put on their entry and no subsidies granted to home producers—especially if the demand is to be increased by the adoption of a 'full employment' policy. Some restriction, at any rate for some time, there will have to be; but it is greatly to the interest both of Great Britain and of the agricultural producers throughout the world that it shall be as little as possible, and that the maximum of opportunity shall be given for foreign trade to expand.

In this connection, United States policy is evidently of crucial importance. At present, the American State Department shows a strong disposition to preach to other countries the wickedness of all forms of what it calls 'discrimination'—a word which it often appears to use in so wide a sense as to cover almost anything a country can do to limit its imports, except by a straight tariff. Such a tariff happens, of course, to be the method employed, with highly restrictive consequences, by the United States itself, or it is difficult to see why it should escape the ban. In truth, there could be no bigger contribution to the expansion of world trade than the sweeping away of the American tariff and the free admission into the United States of all the imports the American people then chose to buy. But this is not in the least likely to happen, not because the United States could not afford to pay for the imports, but because American industry has grown up behind a high tariff wall, and would be thrown into chaos if this wall were suddenly and completely knocked down. Something a long way short of complete removal would of course be enough to give an immense fillip to world trade; but will even this something less be done in face of the fierce opposition which vested interests are certain to offer?

A second condition which is of vital importance for giving international trade a good start after the war is that countries whose economies or whose currencies have been disorganised by war conditions be given promptly the means of buying imports for the rebuilding of their economic life, as well as for meeting their immediate needs for food, clothing, and other necessaries. They must be given these means before they can begin to build up means of their own by the sale of exports; for the imports are needed before the exports can be made. This is the purpose of that part of the Keynes international monetary plan which provides that each country shall be started off with a substantial credit in international purchasing power created by the proposed new International Bank, or 'Clearing Union'. Keynes proposes in effect that this International Bank shall start out by making money out of nothing in much the same way as national Central Banks make money out of nothing. This new money would then serve the purpose of providing an immediate reservoir of effective demand, on which all countries could draw according to the size of their pre-war shares in international trade, or to some other agreed formula. This is the monetary part of an international policy of 'Full Employment'. It will not be effective by itself; but just as in each country an increased supply of bank money is needed to finance an expansion of employment, so an increased supply of international money will be needed to finance 'full employment' over the world as a whole, at all events if it is to be accompanied by a growth of international trade, as it clearly ought to be. As against this, the 'White Plan' produced in the United States and issued by the American Treasury at the same time as the 'Keynes Plan' was issued by the British Treasury, seems designed to force the world back into a state of deflation instead of providing the finance for a policy of expansion. It is so drawn as to drive the world back to the gold standard, and to give the forces of world trade no such flying start as Keynes's *fiat* money would provide—no doubt because the United States holds most of the world's gold stock and the American Treasury is more intent on keeping up its value than on bringing about an increase in the world's real wealth.

This is no place for any full examination of the 'Keynes' and 'White' Plans, to which neither the British nor the American Government is at present committed. What I am pointing out is that, if countries are not to be driven even against their will into drastically autarkic policies on the morrow of the war, means must be found of starting them off all in credit in their mutual relations, and therefore all in a position to buy. Of course, this can only give them a start. In the long run a country can buy only what it can afford to pay for with its own exports, past, present, or future—past, when it buys by selling foreign investments built up by its past exports; present, when it buys with current exports; future, when it borrows capital from abroad on the strength of its future exports, with which it is expected to repay the loans over a period of years. No monetary plan can in the long run enable a country to buy more than it is expected to be able to pay for—though of course the expectation may be wrong. Anything it gets beyond its means of paying is in effect a gift.

A plan, however, which starts every country off with a supply of international purchasing power, created on the strength of the world's productive capacity, may give world economic policies just the required twist away from *autarkie* and towards an expansion of international trading relations. That this should happen is of paramount importance to Great Britain—which is doubtless the reason why the British 'Keynes Plan' gives it the place of honour.

Given the two essential conditions of favourable international arrangements for the encouragement of world trade and a willingness on the part of the other leading countries to take advantage of them in pursuing policies of 'full employment', it should be practicable for Great Britain to achieve a great expansion of exports and thus to be able to keep its position as the principal market in the world for many of the main products of the agricultural countries. It is often not realised to what an extent Great Britain has been the main, and in some cases practically the sole, market for products on which the entire prosperity of certain of the agricultural countries depends. The shutting down of Great Britain as a market would confront these countries with gigantic problems of economic reorganisation, under conditions which could not but lead to a great strengthening of tendencies towards *autarkie* over the whole world. Given reasonable initial conditions for the expansion of world trade in general, there should be no reason for this to happen. Great Britain will need after the war, not merely as much food as before, but more. Even if the increase in demand is met by an extension of home output, particularly of milk and other protective foods, the maintenance of the pre-war demand for food imports will enable the agricultural countries to set their houses in order without too great a strain.

But, it may be objected, Great Britain will not be able to find markets for enough exports to make possible the maintenance of pre-war imports unless wages are reduced in the export trades and in the trades which supply their materials, in order that British exports may be able to make their way by cheapness in comparison with foreign products. It is, of course, perfectly true that the demand for British goods will depend on the prices at which they are offered, as well as upon the total ability of the buying countries to pay for imported goods. Exports must be sold at competitive prices, or they will not be sold at all, except where the exporter is in a position to exert a special pull over the buyer. Great Britain in the past has often enjoyed such a pull, both because investments of capital overseas often continue to influence the direction of the demand for capital goods long after they have been made, and because there is a natural readiness to oblige the principal buyer of a country's exports, and this readiness can be prodded when it does not display itself enough without prodding. To what extent the former of these pulls will remain after the war is uncertain: the latter will remain, unless Great Britain travels a long distance along the road to *autarkie*. Prodding, in the form of Ottawa or Scandinavian Trade Agreements, may no doubt become more difficult if the Americans get their way; for their interest is rather in the other way of influencing trade—through investment. But the power of the biggest buyer to secure a favourable reception for its exports is not likely to disappear altogether.

It is, however, likely to be quite inadequate to get an increased volume of British exports sold if the prices are not right from the buyers' standpoint. Does this mean that British industry will be driven, at any rate in its export branches, to wage-cutting as a means of pushing its exports in the world market? Before we conclude hastily that it does, let us bear in mind that it is not easy to cut the wages of persons who are working for export without cutting wages for many of those who are producing for the home market. Exports and goods for home use are not two different sorts of goods, made by different sorts of workers. They are largely the same sorts of goods, made by the same persons. Wage-cutting for the purpose of cheapening exports, moreover, will not be effective if it is limited to the finishing stages of manufacture: it will need to stretch back into earlier processes as well. At each step it will involve more and more cutting at the wages paid for products made for home use, until it becomes general, or at most leaves out only groups of workers who are especially 'sheltered' or strongly entrenched in bargaining power. A generalised wage-cutting is, however, as we have seen, calculated to do severe damage to demand in the home market, for capital goods as well as consumers' goods; and it is likely that the damage done in this way will greatly exceed the gain in exports and cause a return to unemployment and depression in the economy as a whole. It cannot, of course, be denied that wages can be at a higher level than an economic system can stand, in view of its total productive power, or that high wages may be an obstacle to exports of products which are made in other countries by low-wage labour. There are occasions when reductions in money wages are needed, unless it is deemed preferable to leave money wages as they are and operate on real wages by deliberately raising the supply of money instead, beyond the amount required to sustain 'full employment' at the existing levels of prices. But this is true only when wages are already out of adjustment to other prices: and the admission that such a situation may arise is no sort of an argument for trying to boost exports by means of an all-round cut in money wages.

What, then, is to be done if the cost-prices of British exports are too high to enable enough of them to be sold in the world market to meet the bill for imports? Setting aside the point that reduced wages may so reduce output that wage-costs become higher than before, let us observe in passing that the effects of even considerable wage-cuts on selling prices are often grossly exaggerated. They vary, of course, from case to case according to the proportion of labour-cost to total costs in the industry concerned; but in most cases, except that of coal, which is a primary industry, large cuts in wages will not reduce prices greatly unless they are carried back through all the stages of production or unless capital costs are cut as well. It has been calculated that, over a certain range of cotton piece-goods, it would have been impossible for Lancashire to compete with Japan even if the Lancashire weavers had been willing and able to work for no wages at all.

The alternatives to wage-cutting, as means of cheapening goods to foreign buyers, are reductions in capital charges, increased productive and merchanting efficiency, subsidies, and currency depreciation. Reductions in capital charges, however, are not of much effect at the margin, where prices tend to be settled, except where an industry is working under monopolistic conditions. Increased efficiency must also be secured in such a way as to apply at the margin, if it is to produce its effect. It must eliminate the inefficient producers, without increasing costs by compensation payments to displaced firms, and it must prevent the remaining producers from adopting monopolistic methods. Subsidies, if they are given, must be given in such a way that they are passed on where they are needed, and do not involve gifts to a great many persons who do not need them at all. Finally, currency depreciation, like subsidies, is a game that more than one can play it, and is very likely to provoke retaliatory measures, unless it can be defended with sound arguments, and even when it can. Nor should it be forgotten that currency depreciation renders imports dearer as well as exports cheaper: so that it may do nothing, or even less than nothing, to increase a country's power to purchase imports by means of exports.

What this comes to is that increased efficiency is the thing to aim at, with subsidies in reserve if it is really impracticable to sell enough exports in any other way. Efficiency, however, is not simply a matter of good management, good machinery, and labour skill; it is also a matter of achieving the most economical selling organisation that can be devised, of eliminating all unnecessary intermediaries, and, last but not least, of selecting the most hopeful lines in which to compete. British industry cannot hope, with or without wage-cuts, to compete with countries in which wages are very much lower in lines of production which demand very little skill and can be as well mass-produced by newly broken-in workers just off the land in primitive countries as by workers with generations of high industrial experience behind them. Such a country as Great Britain can hope to expand its exports only by specialising on the types of goods which it is best able to produce; and these are, in the main, quality goods needing a high proportion of skilled labour and technical expertness in their manufacture. Among such goods are both the higher qualities of consumers' supplies and most kinds of capital goods; for most capital goods still need a great deal of skill in both design and execution.

Now, in the post-war world, the demand for capital goods seems likely to be for a considerable time exceedingly high. It seems probable that many backward countries will be making great efforts to lift themselves to a higher economic plane, in order to get the means of employing their redundant populations from the land and of raising their standards of living by producing for themselves the simpler kinds of consumers' goods. The raising of agricultural standards will also mean a big demand for capital goods—not only tractors and other agricultural machines, but also improved means of transport for getting goods to market, and supplies of electric power both for agriculture and for country industries and rural living amenity. There will, no doubt, be an initial period during which such goods will have to be supplied on lease-lend terms, or with the aid of international credits, to buyers who will be without means of immediate payment in their own goods. But it seems reasonable to suggest that the future capital development of backward areas will be carried out much less than past development has been by international long-term lending, and much more by the exchange of capital goods from the more advanced areas for foodstuffs and other raw products from the areas principally engaged in primary production. Doubtless, there will be long-term loans as well; but Great Britain, in view of its high need for imports, will be much less interested than hitherto in investing money abroad, and much more interested in swopping capital goods for necessary foodstuffs and materials.

It is sometimes argued that this process of supplying capital goods to the more backward countries is a form of economic suicide for the more advanced, because it destroys their own markets. This is a mistaken view. The prospects of expanding trade for the more advanced countries depend on the continuous improvement of standards of living in the less advanced. As these countries develop industries of their own, for as far ahead as it is at all profitable to look at present, their demands for the products of the already industrialised countries are likely to increase, provided that the latter countries continually adapt their economic structures to fit in with the changing character of this demand. These more backward countries need, in the earlier stages, principally capital goods designed to enable them to equip themselves with modern power and transport services, to make use of their mineral resources, to raise their standards of agricultural production and to engage in preliminary processing of extractive and agricultural products, and to meet the needs of their own populations for the simplest and cheapest kinds of consumers' goods which can be produced with only a small proportion of skilled labour. These demands will serve to keep busy for the time being the machinery-making industries of the advanced countries; and as the backward countries become more productive with the aid of these capital goods they will become willing and able to buy a wide range of consumers' goods of higher quality, such as are at present beyond the reach of all except a tiny upper class among their inhabitants. I know it can be argued that, logically, this process must end in the industrialisation of all countries, and the disappearance of the system of exchanges between agricultural and industrial countries—unless indeed price-ratios are so altered to the advantage of agriculture as to give the agricultural producers the world over as high a standard of living as the industrial producers. But what sense is there in trying to look so far ahead? If for a long time to come the economic development of backward areas is likely to expand rather than contract the markets open to the producers of the higher qualities of industrial goods—and I do not see how anyone can dispute this—the obviously sensible course is to go all out for this kind of industrialisation, and to leave future generations to face their own problems as we have to face ours. Logical conclusions are mostly nonsense, anyway—and not least so in the field of long-run economic prognostication.

What, then, we ought to aim at is the most rapid possible advance of productive power, both agricultural and industrial, in the more backward parts of the world, from the border countries of Eastern Europe to China, and from the Mediterranean to the whole of Africa. All these countries have, equally with ourselves and the United States, their problem of 'full employment', even if they have not been suffering from unemployment in the ordinary sense of the word. They have been underusing their resources, from lack of knowledge and technical skill, from lack of capital resources except those directed by foreign companies for the benefit of foreign shareholders and not of the countries in which they are placed, and from pressure of population upon the land due to rising survival rates and diminished opportunities for emigration. They have been riddled with 'concealed unemployment'—with persons working, chiefly on the land, whose labour has added little or nothing to the volume of production; and they have, of course, suffered wretchedly as a result of the failure of the more advanced countries to keep any control over the forces of epidemic depression. For all these countries, 'full employment' is a matter of extending capital resources and improving productive technique; and one form of export which could be extended to them with great advantage is the export of technical skill, not so much to operate their plants for them as to teach them as speedily as possible how to operate them for themselves. I can imagine no better form of lease-lend export from the advanced countries in the period of reconstruction than an export of technicians and technical teachers, accompanied by the plant which they will teach the peoples of the backward countries to operate with success, and thus to pay for out of the increased product of their own better-directed labours.

Unless this is done, the stimulation of 'full employment' in the industrial countries, and especially in Great Britain, will encounter quite unnecessary obstacles. For, if the advanced countries do not export capital goods to the backward countries in payment for needed imports, what are they to export? The inhabitants of the backward countries are too poor to buy the consumers' goods which the advanced countries would like to sell them, and will remain too poor until their equipment of capital goods and technical skill has been increased. If it is objected that economic development in the Soviet Union has not meant active trade between the Soviet Union and the capitalist countries, whose fault has that been? The Soviet Union has been compelled to carry through a process of intensive industrialisation with a minimum of external aid; but if such aid had been forthcoming on tolerable terms the sufferings of the Soviet peoples in the course of the transition would have been immeasurably less and depression and unemployment in the capitalist countries would have been a good deal less severe.

It is indeed evident that a 'full employment' policy will work best and most easily if all the world is in it—advanced and backward countries together. If, among the economically advanced countries, one or more should refuse to play, the necessity of bringing in the less advanced countries will be even greater than it would otherwise be. If, for example, the United States were to refuse to play, it would be even more necessary for Great Britain to look for an extension of reciprocal trading relations with the East, with Africa, and with the less developed parts of Europe. It would be a great calamity if the United States were to refuse to play, or were to attempt to impose terms, based upon purely American needs, which other countries could not possibly accept. For such a refusal would mean depression and crisis in America, and America looms so large in world economic affairs that the existence of depression there would require much more drastic action than would otherwise be needed to prevent it, and to sustain the level of employment, elsewhere. Even so, I believe, the thing could be done; but there would be much more danger of Governments taking fright at the magnitude of the task, and failing because they were afraid.

The danger, put in a few words, is that the Americans may seek to fasten on other countries a pattern of world trading relations and international finance that these other countries may not be able to fit into, however hard they may try. For example, the Americans may want, having superabundant supplies of gold, to restore the gold standard everywhere in order to find an outlet for these supplies. But it may be as disastrous as it was after the last war for countries to fix absolutely the relative values of their currencies, above all before they have had a chance of finding out what relative values fit in best with their internal economic conditions—their price and wage-structures, the status and contractual position of capital-ownership among them, and so on. Nor will it be less disastrous if, in the name of 'freedom of trade', the Americans leave themselves free to keep their tariff as high as they please, but try to prevent other countries from entering into mutual trading arrangements which will enable them to conduct exchanges that would not occur at all if 'bilateralism' were strictly tabooed. Again, what if the Americans, intent on preserving the capitalist order, take a stand against State trading, even where bulk supply and bulk purchase are the best ways of arranging for the orderly production and exchange of goods between two countries with complementary resources? I do not say that the Americans will act in these ways; but it will need world imagination and high persuasive power on the part of the leaders of American opinion to prevent them from wrecking their own prospects of economic stability by abuse of their vast economic power, which will be at its most preponderant in the period when the peace settlement is actually being framed.

CHAPTER XI

'CONSUMERS' CREDITS'

I HAVE no doubt that, throughout the foregoing chapters, a number of my readers have been impatiently looking for some discussion of other means of stimulating consumption than the maintenance of wages and the institution of public works of capital construction. 'Why not consumers' credits?' I am sure some of them have been asking.

What exactly does this question mean? A 'credit', in the ordinary use of the word, is a loan, and is meant to be repaid. Bank credits and trade credits are alike in this: they are loans, and fall due for repayment at the end of a specified period. They may be renewed, but are not cancelled save in the case of the bankruptcy or failure of the borrower. Normally they bear interest for the period for which they remain outstanding. Do those who favour 'consumers' credits' as a means of abolishing unemployment mean merely that in bad times consumers should be *lent*, at interest, money which they will have to repay later on?

Those whom I have met or read seem to mean something very different. They seem to mean that, either as a normal practice or exceptionally in bad times, the State should create money out of nothing and make a present of it to the citizens with the object of raising the level of consumers' demand and thus getting unused productive resources into employment. Some of them suggest that there is a permanent tendency in capitalist societies towards a deficiency of purchasing power, which needs to be made good continually by the issue of 'consumers' credits'; while others hold that this deficiency arises only at particular times of economic depression. Let us begin by considering the less extreme opinion—that at certain points in the economic conjuncture there arises a deficiency of purchasing power that can best be made good by the issue of gifts of newly created money to the consuming public.

It is of course undeniable that deficiencies of purchasing power exist in bad times; for purchasing power arises from only two sources, the acquisition of incomes through production[1] and the loan or gift of newly created money. If unemployment of resources exists, one source of purchasing power is *ipso facto* reduced; and, as matters have stood hitherto, this reduction has tended to cause a reduction in the other also. Banks' power to

[1] Including, of course, the transfer of incomes arising in this way by means of gifts, or re-distributive taxation.

lend is limited by the willingness of credit-worthy borrowers to borrow; and few persons appear credit-worthy, and such persons wish to borrow less, when production and trade are depressed. There is no dispute about the existence in bad times of a deficiency of purchasing power, or, I think, about the further point that at such times some of the reduced supply of purchasing power tends to be withheld from use, thus reducing the supply yet further. The question is whether the best remedy is to put additional purchasing power directly into the consumers' hands.

There are two main ways in which this can be done. One is simply to issue so much additional money income to every consumer, or to certain classes of consumers, providing the money by creating it out of nothing, in the same way as bankers create their credits, but with the difference that, unlike bank credits, it does not bear interest and is not meant to be repaid. The alternative way is to reduce the level of taxation, and to meet the current expenditure of the State and other public bodies by creating new money instead of transferring money for this purpose from private incomes to the public. The effect of this is to leave more money for spending in private hands—in whose hands depending on the form which the tax remissions take. This money may be repayable or not. If it is meant to be repaid, the method will be for the State to raise the level of taxation in good times beyond what it would otherwise have been, and thus to recover from the taxpayers the amount remitted when times were bad.

I

Tax remissions will affect the situation differently according to the distribution of the benefit. To the extent to which they add to the spending power of the poor they will tend to raise consumption by the greater part of the amount remitted; but to the extent to which they accrue to the rich or to companies and other collective institutions the stimulus to consumption will be much smaller, and the stimulus to 'saving' much greater. Will an increase in 'saving' under these conditions be reflected in an increase in real investment in capital goods, or be merely "spilt on the ground"?[1] There will not be an increased willingness to invest in capital goods unless there is a noticeable stimulus to consumption. Remissions of taxation granted to rich people (e.g. remissions of taxation on company reserves and large incomes) will not noticeably stimulate consumption, and will not, therefore, stimulate investment either. If tax remission is to be used as a method of reviving demand and increasing employment, it must be concentrated mainly on decreasing taxation on

[1] See page 50.

the smaller incomes. The stimulus given in this way to consumption will of itself stimulate investment, without any need for presents of tax remission to the richer classes—that is, on the assumption that the banking system stands ready to increase the supply of money to the required extent.

If taxes are remitted in this way in times of heavy unemployment, should they be raised correspondingly in good times, in order to recover the sums remitted? If the State has borrowed at interest from the money market the sums required to cover its expenditure no longer covered by taxation, it will need at some period to recover from the taxpayers the amount needed to wipe out the debt; for otherwise every depression will leave behind it a permanent addition to the National Debt and to the annual interest charge upon it. This method of borrowing in the slump—thus taking up idle funds which would otherwise not be invested—and repaying out of higher taxation in the boom was the method used by Sweden in the 'thirties in financing its public works policy; and it worked perfectly well as far as it went. It is, however, a somewhat different matter for the State to borrow, not for capital works, but for the issue of additional incomes to consumers; for in the one case the State possesses the capital works as an offset to the debt, and in the other it possesses nothing. It is perfectly orthodox finance to spread payment for capital works over a period of years by means of a sinking fund; and this is in effect what is done when the State borrows for such works and thereafter gradually pays off the loan. Borrowing to finance current consumption is not orthodox finance: it is regarded in private affairs as characteristic of the spendthrift. If the State resorts to it, surely, it will be argued, there ought to be the fullest assurance that the money will be repaid as soon as the community is well enough off to afford it. It need not be repaid by the individual consumers to whom it has been given; but it will have to be recovered from somebody by way of a higher level of taxation.

This, however, like so many of the common analogies between the individual and the State, is misleading. If the State, having emitted money in order to bring unused productive resources into use, proceeds later to recall it, what can the effect be except to throw the resources again out of use, and bring back the depression? If, indeed, depression is a quite irrational force, come to-day and gone to-morrow, this may not be true, and the State may be able to withdraw and annihilate the money created in the depression without adverse effects. This, however, is not the case. The additional money will be needed to keep the level of employment up; and, if the State withdraws it, either depression will return or the money previously made available by the State will be replaced by new money created by the banks. This latter is what will actually occur, under normal circumstances. If the State taxes the people heavily, in order to repay the debt, the banks will step in with additional bank loans, as long as they see a prospect of finding credit-worthy borrowers. If, however, the State levies its increased taxation to any considerable extent on the poor, consumption will fall off, and the willingness to invest will fall off with it; and the banks will not be able to find borrowers to take up the new money. In that case, depression and unemployment will return.

What will happen if the State provides the money for its current expenditure, to offset tax reductions, not by borrowing but by creating additional funds? These funds will be spent by the State in the same ways as the proceeds of the remitted taxes would have been spent, and will affect consumption and investment in the same proportions as they would have been affected if the money had been raised by taxation. The State will have anything to show for them only to the extent to which it was previously, if it was at all, paying for capital works out of current revenue. The new money goes into circulation as an addition to the money previously in circulation, and accordingly the increased level of economic activity does not give rise to the same need for an increased supply of money from the banks. The State money replaces the bank money: in effect the State has gone into banking and has granted to itself interest-free loans instead of borrowing at interest from the banks.[1] Must the State repay itself this money, as it would have had to repay the banks? No, it need not, if the increased supply of money will be needed permanently to sustain the higher level of economic activity. But each act of creating money out of nothing and then spending it to meet public charges is a *permanent* addition to the supply of money. The money can be spent into existence once only, not again and again. The banks can go on granting credits again and again, because their credits are continually being repaid. If the State does not repay, it cannot spend into existence any more without a fresh *permanent* addition to the monetary supply. Moreover, to the extent to which the State makes such permanent additions, it deprives the banks of the power of making them, and of earning interest by doing so. The bankers are therefore tempted, in order not to lose their profits, to issue, up to the limits of their ability, more money than they would otherwise have done. The State issue of money has an inflationary tendency, not directly but through its reaction on the banks. In bad times, as we have seen, the banks can do little to force additional money

[1] See pages 119 ff.

into circulation; but when 'full employment' exists, or in fairly prosperous times, they can do a great deal, unless they are stopped by legislation. Therefore, if the State took to making its own money while leaving the banking system unfettered in private hands, the consequence would be monetary inflation, to which the bankers would resort in order to restore their profits.

The State could prevent this, by taking full control of the Central Bank, which, in modern systems, effectively controls the total supply of money. But this would mean, in effect, that the State, instead of making its own money independently of the Central Bank, would make it through the Central Bank, on lines which I have discussed in an earlier chapter.[1] The case of the State financing a budget deficit, due to tax remissions, by the use of its own 'credit', turns out to be the same as the case of the State taking over the Central Bank, and thus assuming the right to make its own money.

To the extent to which the Central Bank has to provide interest-free money for the State, instead of providing interest-bearing money for the business world, the Bank makes a loss instead of a profit; for it must cover its administrative charges. If the State covers these charges, the Bank still loses profit it would have made on interest-bearing loans which it is no longer able to make. The effect, however, of the State's action in increasing economic activity may be so great that the volume of interest-bearing money the Bank is able to create may be greater than the total amount of money it would have been able to create if the State had stood aside. It may, therefore, even make a higher profit than before. Whether this will be possible will depend on the relation between the magnitude of the State spending out of new, interest-free money and the total addition to the supply of money that is needed to induce a condition of 'full employment' in the economy as a whole.

The conclusions to be drawn from the foregoing discussion are (1) that tax remissions, and an unbalanced budget in bad times, can stimulate economic activity and employment, but that (2) they will do so only if the remission is mainly for the benefit of the *lower* income groups; (3) that, if tax remissions are financed by borrowing, and the loans are repaid by increased taxation in good times, depression will ensue on the repayment unless the compensating taxes are levied mainly on the *higher* income groups; (4) that if the tax remissions are financed by State issues of money, and not by borrowing, the effect will be to transfer a part of the profit of money-creation from the banks to the State, and to set in motion counteracting inflationary tendencies unless

[1] See page 121.

the Central Bank is taken over by the State; (5) that if the Central Bank is taken over, the effect is that the State acquires a virtual monopoly of the power to create money, either for its own use without interest, or for the use of the business world at interest; (6) generally, that the policy of tax remissions and unbalanced budgets in bad times is not in itself open to condemnation on any valid economic grounds.

The alternative to tax remissions is the direct grant to consumers of additional purchasing power. This in the final resort amounts virtually to the same thing. The consumers in either case have more money to spend; and the State has either to borrow this money or to create it—for we need not consider the case in which the State raises the money by additions to current taxation, as that would clearly but *transfer* purchasing power and not increase it.[1] Just as tax remissions will vary in their effects according to the ways in which different classes benefit, so direct grants of purchasing power will vary according to the same principles. If it is easier to make sure of the poor benefiting by making direct grants than by remitting taxes, direct grants are the better way. As for repayment, direct grants can be refunded by increased taxation in good times just as easily as tax remissions, if it is desired to do this; and here again the same conditions apply.

2

So far, we have been confining our attention to proposals designed to increase consuming power *in bad times only*, and not at all times. It can of course be said that a deficiency of consuming power exists at all times at which total economic activity falls short of 'full employment', and that accordingly 'consumers' credits' should be issued at all times, in varying amounts up to the total needed to achieve 'full employment'. On this view, there could be no question of repaying the credits, unless there were periods at which the level of employment exceeded 'full employment', or prices were being forced up because there was more purchasing power in existence than was needed to sustain 'full employment'. Such a situation could arise only through a mistake in allowing too much purchasing power to be issued; and obviously the right remedy would be to reduce the amount to the required level. Such mistakes apart, there would be no 'surplus' years in which the 'consumers' credits' issued in years of 'deficiency' could be repaid.

What, then, would happen? The State would be continually

[1] Save, of course, to the extent to which a tax transfer from the rich to the poor would increase consumption at the expense of wasted 'saving'.

making new *permanent* additions to the supply of purchasing power. On every occasion on which the demand for productive resources fell *temporarily* below the supply, the deficiency would be made good by a *permanent* addition to the supply of purchasing power. This would evidently lead, on the first application of the policy, to a rapid attainment of the level of 'full employment', whereupon the issue of consumers' credits would stop. The case is so far exactly the same as that of an exceptional creation of consuming power, considered in the first part of this chapter. Thereafter, the additional money created in the first instance would continue to circulate. Let us presume that, later on, renewed recession would set in owing to the endemic tendency of the capitalist system to breed underconsumption.[1] The result of this would be to reduce the total supply of money; and, as the State's money would not be reducible, the reduction would have to occur in other kinds of money created by the banks. The State would then step in with a new creation of money, and the process would be repeated. What would be occurring at each stage would be a diminution in the proportion of interest-bearing bank money to State money in the total supply until the State money had completely ousted the bank money and comprehended the entire monetary supply.

But how, it will be asked, could this possibly happen? If industries were to remain in private ownership, somebody would have to provide the owners with credit, or they could not carry on. Unless the State were to take to supplying money to the industrialists, the industrialists would have to go to the money market for it. And, if there were willing borrowers in the market, the banks would be able to command interest for lending them money.

True enough! The increase in the quantity of State money would not stop the banks from lending, within the limits to which they were allowed by law to create money. But if the State fixed the total amount of money at the amount needed to maintain 'full employment', and then proceeded to make more and more of this money itself, it would have to restrict the bankers' power to create their own money in proportion as it increased its own supply. This would not prevent the bankers from lending; for an increasing amount of the State's money would pass into their coffers from their own customers. What it would prevent would be the creation of that superstructure of credit money which the banks, as we have seen, rear upon a much smaller basis of cash. The banker would find himself, to an increasing extent, approaching and at length reaching the point at which he could lend, but no

[1] See pages 46 and 48 ff.

more than the actual amount of cash he held. The profitable business of making bank money out of nothing, and earning interest upon it, would come to an end. The supply of cash would increase until it covered the entire monetary needs of the community, whereas to-day it covers only a fraction. The banks could then create no further credit, and the State's power without inflation to manufacture more State money without inflationary results would be limited to that of providing for any increase in the supply of money that might be needed in future for the maintenance of 'full employment'.

I have assumed in the foregoing argument that the money created by the State would take the form of cash and not of mere book-entries. This assumption is fully legitimate. The State, *ex hypothesi*, would be using the money to pay its bills or to hand out as purchasing power to the citizens. Those who received it would spend it again, and so on in an endless series; and such part of it as was not hoarded in cash would be paid into the banks as deposits, and drawn upon as need required. If the State paid initially by cheque, and its cheques were paid into the banks, the banks could promptly present these cheques to the State for payment; and the State could pay only in cash—that is, in notes —or by the crediting of deposits in the Central Bank, which the other banks, as we have seen, treat as the equivalent of cash, because they are immediately exchangeable for cash. It would make no practical difference whether the other banks continued to hold the State money as deposits in the Central Bank or took them out in cash and transferred them to their own vaults.

I have made a second assumption—that the State's control over the total amount of money (so as to keep it at the level needed for 'full employment') would extend to control over the credit superstructure and not merely over the cash basis of the commercial banks. This is also a fully legitimate assumption; for without it the manufacture of State money constituting cash or its equivalent would lead unavoidably to an inflation of the total supply of money beyond the level needed to maintain 'full employment'. The State could not adopt the policy of 'consumers' credits' of the type we have been considering without controlling the supply of all kinds of money, including bankers' credits.

The conclusion which emerges from this second part of the argument—which has necessarily been at certain points somewhat fanciful—is that any plan involving permanent additions to the supply of money by the State—or of course by any other agency—must be accompanied by a parallel power to enforce contraction of the right to create money of any sort from any other source, if the result of the emission of the new money is not to be inflation. The particular form which this contraction would have to take under existing banking systems would be a contraction of the superstructure of credit which banks are able to raise on any given cash basis; and the effect of this contraction would be to make private banking unprofitable unless it were left open to the bankers to drive rates of interest up and up in order to recoup themselves for their loss of lending power. If they were left free to do this, the rise in interest rates would become deterrent to borrowers, and the further decline in lending would again make banking unprofitable. It is, however, clear that the State could not allow interest rates to rise in this way. In effect, the assumption by the State of the right to issue its own money up to the level required at any moment to sustain 'full employment' would, if the money were not made repayable (which we are assuming at this stage of the argument), inevitably bring private banking to an end by making it unprofitable. The plan would therefore have to include the taking over of the banks—the commercial banks as well as the Central Bank—by the State.

If the banks were taken over, there would be nothing to prevent the State from following, if it so desired, a policy of 'consumers' credits' constituting permanent additions to the supply of cash, up to the total needed to equip the community with a money supply adequate to sustain conditions of 'full employment'. But an increase in the supply beyond this point would necessarily produce inflationary consequences.

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So far, so good. But we have still to ask whether the policy of issuing 'consumers' credits' is or is not a *sensible* policy, even if we admit that it is perfectly practicable, within certain limits. The effect of such a policy is to act directly on the level of demand for consumers' goods and services, in the expectation that this will react on the demand for capital goods by making business men readier to invest in them. This means that the demand for consumers' goods is stimulated immediately, whereas the demand for capital goods increases only as a result of it and therefore after some lapse of time. Even if the interval is short, the additional demand for consumers' goods takes effect a considerable time before there can be ready any additional supply *made with the aid of the new capital goods*. This does not mean that there can be no increase in the supply of consumers' goods and services until the new instruments of production are in use; but it does mean that any earlier increase must be the product of the capital goods already in existence before consuming power was increased.

There are two disadvantages in this. In the first place, there may be a considerable rise in the marginal cost of the additional consumers' goods, due to the bringing back into full use of relatively obsolete productive instruments or the working of more efficient instruments beyond the *optimum* point (e.g. systematic overtime). Up to a point, this tendency may be counteracted by the effect on costs of the fuller working of instruments of production which were previously being operated below the optimum level; but where monopolistic forces possess much strength the tendency to transform such reductions into windfall profits will be powerful, and the price-levels of consumers' goods will tend to rise sharply.

Secondly, the immediate rise in consumers' demand, before new instruments of production can be brought into use, will tend to stimulate the demand for imports, and thus to magnify the foreign exchange difficulties in the way of a national policy of 'full employment'.

It is of course likely to be generally the case that the new instruments of production, when they do enter into operation, will be more efficient than many of the existing instruments. This will tend to drive some of the older instruments out of production, and to lower costs at the margin, provided that the supply of new instruments is large enough to supply the expanded market without retaining *all* the older instruments as well—as it will usually be.

As against these effects of 'consumers' credits' let us now consider what will happen if the State's policy is directed rather to increasing the supply of capital goods than to the direct creation of additional consuming power. In this case also there will be an increase in consuming power, through the sums paid out to the producers of the capital goods. But the production of the additional capital goods will begin at once, without any time-lag, and the consumers' goods produced with the aid of the new capital goods will therefore come sooner on the market to check the rising tendency of costs and prices in the consumers' trades.

There is, moreover, a second advantage. Unemployment of men and other productive resources will be a good deal worse in the industries producing capital goods than in those producing consumers' goods (except for export), and there will be accordingly in the capital goods industries much more reasonably efficient plant and skilled labour ready to be called back into employment. There will be many more cases in which real costs will fall with the employment of this plant up to the *optimum*, and under these conditions the rise in prices will at any rate be smaller than where real costs rise, even if it cannot be altogether prevented.

The action of the State will thus impinge on those parts of the economic system which most need stimulating; and a more balanced and easier recovery in the level of employment will be possible.

There is, to be sure, a very important qualification which has to be made. If the State's public works policy is of such a kind as not to stimulate the production of the kinds of capital goods that will produce the kinds of consumers' goods and services on which the consumers will desire to spend their increased incomes, the results here ascribed to the policy of stimulating the capital goods industries will not follow. If, for example, the State builds immense numbers of roads, post offices and public buildings, and nothing else—as it may be tempted to do because these types of public works will arouse least opposition from private capitalists—the producers of these things, when they come to spend their additional incomes, will not find in the market, or expected to come into the market, additional supplies of what they want to buy, manufactured by new instruments of production, save to the extent to which private investment has already reacted to the State's expansive policy by erecting new factories of its own for supplying these expected wants. The results of a *narrow* public works policy of this kind will, therefore, be the same as the results of a direct creation of 'consumers' credits', except that the State, for its public works, will have withdrawn from the labour market a certain number of workers who would otherwise have been looking for private employment on jobs not ordered by the State.

We have seen earlier that a public works policy for stimulating production and employment must, if it is to work well, be framed on *broad* lines, so as to give a direct stimulus to production over a wide field, and especially to as many as possible of the actual industries which are most seriously depressed. It must do this if its employment policy is not to be hampered by structural maladjustment to a much greater extent than there is any need for it to be. A *narrow* policy of public works has only the advantages over 'consumers' credits' that it directly reduces the numbers unemployed by the numbers employed on the State works and that it presents to the community in return for its expenditure the value of the works when they are done. A *broad* policy of public works has the additional great advantage that it can operate precisely at the points at which the industrial system is most distressed; and can expand employment with the minimum of geographical or occupational migration, the minimum scrapping of resources that are not obsolete, and the minimum sacrifice of existing skills.

In general, the balance of advantage is plainly in favour of public works as against 'consumers credits', as the main policy to be followed. This, however, need not exclude the use of 'consumers' credits' as an auxiliary measure; and it certainly should not exclude the policy of tax remissions and unbalanced budgets in bad years. Such measures are eminently desirable, as auxiliaries, provided that they are rightly adjusted to the need—that is to say, provided that the tax remissions benefit mainly the *lower* income groups and that any recoupment of the sums remitted falls in the good years on the *higher* income groups. Taxation rearranged on a counter-cyclical instead of an annual basis does not shed its need to be re-distributive as between rich and poor; nor can it, as long as we live under an economic system which tends continually towards maldistribution and underconsumption.

Note.—There is, in some quarters, a predilection for confusing the policy of 'consumers' credits' with the policy of 'social dividends', or 'incomes for all', apart from the incomes paid out as rewards to the owners of the factors of production: They are not, however, the same. 'Social dividends' could, of course, be paid in the form of 'consumers' credits' out of State-created new money; and what would happen if this were done I have tried in this chapter to show. But 'social dividends' could also be paid, as it is proposed in the Beveridge Report that children's allowances should be paid, out of the proceeds of general taxation. I agree that it would be very difficult to do this on an adequate scale under the capitalist system. But 'social dividends' could quite well be paid, under a Socialist of semi-Socialist system, by the method of dividing the income generated in production into two parts and paying out one part in rewards to the producers and the other in the form of a general 'social dividend'. This is the form in which I have advocated 'social dividends' in my earlier writings. (See *Fifty Propositions about Money and Production* and *Principles of Economic Planning*.)

CHAPTER XII

SOCIALISATION, PRIVATE ENTERPRISE, AND PUBLIC WORKS POLICY

At the conclusion of the preceding chapter, a contrast was drawn between a *narrow* and a *broad* policy of public works, and emphasis was laid, as it had been earlier,[1] on the superiority of a

[1] See pages 83 ff.

broad policy. My final task is to endeavour to examine more closely than I have done so far what such a policy involves in the extension of State activity in the industrial field. In order to be armed to follow such a policy whenever and in whatever form the need arises, what must the State take over, and what, without positive acquisition, must it effectively control? How much socialisation is implied, and how much restriction in the scope left for private enterprise is involved?

Let us consider these questions first of all with the conscious omission of one factor, which may prove to be of key importance, but can best be brought in at a later stage. Let us omit the psychological factor, in its twofold aspect of the effects likely to be produced on the minds of business men by an extension of public economic activity, and of the attitude of mind needed in those who are to undertake the new economic tasks on behalf of the State. Let us, for the moment, assume that business men continue to 'play' when the State limits their scope, and that the State succeeds in finding business administrators for its own concerns not inferior to those who are at work at present in private enterprise. I am not asking that these things be taken for granted —far from it: I am merely deferring discussion of them for a few pages.

A large proportion of the normal demand for new capital goods is concentrated, under modern conditions, in a fairly small range of industries and services. From the majority of manufacturing trades, the current demand for capital goods is fairly small. This is not, of course, unimportant in the aggregate; but it is very widely diffused. As against this, certain key industries and services use up, in times of general activity, a very high proportion of the total supply of capital goods. Pre-eminent in this group is housing, with its close relative, the demand for civil engineering applied to roads, bridges, and similar public works. Of great importance in this same group is transport, especially railway transport and dock and harbour work and shipping—to which must now be added air transport, of course including airports. With these must be grouped the other main public utility services—electricity supply, water supply, and, to a smaller extent, gas. These industries together form a group, which we may call the 'capital-goods-using' industries *par excellence*. If the rate of demand for capital goods from these industries and services taken together could be effectively regulated, so as never to fall below a certain minimum and to be raised above that minimum whenever the necessity arose, the main feature of cyclical unemployment as it has hitherto existed would disappear.

Closely related to this group of capital-goods-using industries and services is the group of industries which produces the main supply of capital goods for their use. The industries which stand out in this second group are building, civil engineering, the various branches of mechanical and electrical engineering, especially on the heavy engineering side, shipbuilding, and the iron and steel and non-ferrous metal industries as producers of the semi-manufactured materials needed in the group. To these must be added brick, tile, pipe, cement making and other industries supplying builders' materials, and that part of the coal industry which works for these two groups of industries rather than directly for the household consumer. We may call this second group the 'capital-goods-producing' industries.

It is in this second group that, apart from the special case of the export trades, a very large amount of unemployment is usually concentrated in periods of economic depression. But clearly the key to a revival of demand for the products of the second group is to be found in the industries and services constituting the first group. These 'capital-goods-using' industries and services are, accordingly, the key points for the operation of a programme designed to stimulate activity in the field of real investment. This activity needs stimulating in other spheres as well—indeed, over the whole range of industries needing capital equipment for the production of finished goods and services; but as a high proportion of the total capacity to absorb capital goods is concentrated in this particular group, its state of activity is evidently the crucial thing.

It may seem to some persons curious to speak of housing as an industry or service separate from building, and one which the building industry exists to supply. This is, however, the correct way of stating the position. Houses are capital goods, as are of course other kinds of buildings; and the ownership of houses for renting out is clearly as much an industry or service as the ownership of power-stations or water-reservoirs, or anything else which, having been constructed, yields up its capital value to its users, not all at once, but over a long period. Nor is the position essentially different when the houses are nominally sold, either through a Building Society or Insurance Company or bank, or under the Small Dwellings Acquisition Acts, on the instalment plan. In such cases, the bodies which advance the money are in effect in the position of house-ownership until the mortgages have been paid off. In view of the fact that most families cannot afford to buy their own houses at all, and many who do buy can afford to buy only on the instalment plan, there has to exist a service of house-ownership, with a large amount of capital locked up in it; for without this service the building industry would be left almost without customers for its products. This service of house-ownership may be either public or private; and those who own the houses may prefer to sell them outright or on leasehold terms, or to let them at weekly or yearly rents. Generally speaking, new houses to let are often municipally owned, and old houses, dating from the days of speculative building, privately owned; whereas new houses for sale have been during the inter-war period predominantly the province of the Building Society and the Insurance Company. This distinction is by no means absolute; but it broadly represents the situation.

In an earlier chapter, I tried to show why it is to be expected that house-ownership will be after the war increasingly public. Evidently, such a growth in the sphere of public enterprise has much to recommend it from the standpoint of increasing the State's power to maintain and, where necessary, expand the volume of investment in the largest of all the capital-goods-using industries.

Of the demand for civil engineering works closely related to housing it is not necessary to say much; for such works are already predominantly under public ownership, and likely to remain so. There has been from time to time some talk of privately owned toll-roads for the exclusive use of motor traffic; but nothing is likely to come of this. If fast motor-roads are built, it can be taken for granted that they will be publicly ordered and owned. Toll-bridges still exist; but they are dying out. Land drainage schemes are already in the hands of public bodies; and it is the State that protects the coasts as far as they are protected. The care of rivers is indeed divided between private and public responsibility; but any extensive future schemes are certain to be in public hands.

The transport services come next in order of key importance after housing and what is called in the official returns 'public works contracting'. Over a wide range of industries rates of interest may have but little effect on the volume of investment in comparison with variations in the optimism or pessimism of the business world. But in transport, as well as in housing, long-term interest rates do have a considerable effect. There are many works of construction, on the railways, at ports and harbours, and in the building of ships, which will seem worth while if interest rates are low and not worth while if they rise to a higher level. This is largely because, in general, business men concerned in transport undertakings have to think in terms of returns spread over a longer period than business men in most other industries. As it is harder to estimate the course of demand over long periods, their expectations tend to be governed more by the rates of interest absolutely and less by the relation between these rates and their expectations of gross profit. Similar considerations would apply even if the transport undertakings, instead of being run for private profit, were taken over by the State. In view of the difficulty of anticipating the long-term conditions of demand for transport, the public authorities would have to estimate the direct economic worthwhileness of investment in this field largely by considering costs, in which interest rates would play an important part. But it would be practicable for the State, as it is not for private undertakings, to be guided by other considerations besides the direct prospect of profit in deciding how much investment to undertake in the means of transport. The contribution of transport services to general economic prosperity is largely indirect, and is not necessarily measurable in terms of the direct economic yield. The State, if it owned the means of transport, or at any rate those which are the main users of expensive capital goods, would be in a position to regulate and to time the level of investment in transport agencies in a way which is impracticable as long as these services are run mainly for private profit.

Similar considerations apply to the other public utility services —electricity, water, and gas supply. The State, by owning these services, would be placed in a position to determine the rate of capital investment in them so as to fit in with the needs of the community as a whole, and the return on such investment would not be limited to the direct yield from their operation. It would include also the indirect yield arising from the stimulus given by improved public utility services to industrial production generally and to better sanitation and living conditions among the general body of the public.

If the whole range of the principal capital-goods-using industries were placed under public ownership and administration, the State's power to operate a *broad*, as distinct from a *narrow*, 'public works policy' would be greatly increased. Public administration in this field would enable the State to transmit additional orders when it thought fit to the capital-goods-producing industries, and thus to strike directly at unemployment of resources in the worst-affected sectors of the whole economy. It is, from this point of view, much more important to socialise the industries and services which *use* than those which *produce* capital goods; for the control of the demand factor rests with the user, and not with the supplier. There may be other perfectly valid reasons for socialising some or all of the capital-goods-producing industries; but the desirability of following a 'public works policy' designed to promote 'full employment' is not among them, or, it would be better to say, is not among them except to the extent to which they are dominated by restrictive or monopolistic influences that cannot be overcome without public acquisition.

In other words, the case for socialising, in one form or another, the industries and services which are the principal *users* of capital goods rests primarily on the direct power which such socialisation will give to regulate the volume of activity in these fields; whereas the case for socialising any or all of the industries *producing* capital goods must rest rather on the prospect of improving their efficiency and removing the retarding effects of monopoly upon them. It is plainly of importance that, if the State adopts a 'public works policy', it shall not be compelled to pay tribute to monopoly or inefficiency for the capital goods which such a policy causes it to buy. It would, however, fall outside the scope of a book dealing with the problem of 'full employment' to consider how much socialisation is desirable on this latter ground.[1]

What is clear is that the State, in order to be able to operate a *broad* policy of public works, must take over at any rate the main parts of the services of house-ownership, transport, and other public utilities, and must thus constitute itself the arbiter of the level, and of the timing, of investment policy in these fields. I am not suggesting that the State should not go further than this, but only that if it stops short of this point its 'public works policy' will be very likely indeed to break down.

We can now return to the question—or rather the two questions—consideration of which was deferred at the beginning of the present chapter. First, if the State takes over the range of services suggested as a minimum, how will the psychology of business men be affected? Will they be readier, or less ready, to sponsor the requisite investments in other industries and services—requisite, I mean, in conjunction with the investments made under public auspices, to sustain total economic activity at a level of 'full employment'? The answer to this question must depend on what business men *expect* to happen after the initial change has been made. If they think that the State, having advanced just so far in the direction of social ownership, means to stop, at any rate for some time, at that point, and to pursue a policy of stimulating private industry in the fields which it has not taken over, business men will be led by self-interest to 'play', as soon as their hopes of securing an immediate reversal of the State's policy have vanished. They may, for a time, try to stand solid with the vested interests which are being made subject to immediate socialisation —the more so because big business men usually have fingers in many pies, and the same persons will hold leading positions in

[1] For a consideration of this problem, see my *Great Britain in the Post-war World* (Gollancz, 1942).

industries and services that are, and that are not, to be taken over. But this solidarity of the capitalist world will not endure for long if it is apparent that the State has no immediate intention of socialising further industries on any large scale, and that it does intend to ensure that the expansion of total demand and of the monetary means accompanying it shall be maintained. The prospects of profit which these conditions offer will be too attractive to be neglected for long out of private resentment at the State's invasion of fields formerly reserved for 'private enterprise'. The business world, even if it holds off for a time, will presently begin to 'play', provided that the Government sticks firmly to its policies through the period of initial difficulty.

Even if socialisation extends to a number of the capital-goods-producing industries, as well as to the industries and services which are the principal users of capital goods, the same principles will apply, though the resistance of the business world will probably be in that event stiffer and more prolonged. In the long run, business men will not forgo good prospects of profit merely because they do not like the thought that the State is creating these opportunities by entering into business itself.

What, however, of the other psychological aspect of the kind of 'public works policy' which has been recommended in this book? Will the State be able to find administrators who will run publicly owned and managed industries as efficiently as they would have been run by private enterprise had the State not taken them over? To anyone who has had much experience of Civil Servants this is a question that is bound to raise doubts. The typical 'high-up' Civil Servant is by no means lacking in intellectual ability. Like 'dons' he is clever; but he shares many of the outstanding qualities of the academic mind—pernicketiness about details, extreme timidity in action, and difficulty in co-operating in any work which needs the joint effort of a considerable number of minds. In speculation he may be (or he may not be) audacious: in action of any novel sort he almost always hangs back. He likes marking out for himself his own defined sphere of activity, and dislikes any uncertainty about the frontiers of his own and his colleagues' spheres. He is fussy, old-maidish, and addicted to routine; and he feels an instinctive hostility to persons whom he regards as adventurers—that is, to anyone who pushes on in action further than he has proved in thought that he can securely go. This type of mind, however admirable for certain purposes, is about the worst possible for having anything to do with the essentially adventurous business of running the world, or, to be more specific, taking charge of an industry which is bound to be in constant need of adaptation to changing forces of technical knowledge. If there is anything clear in a dark world, it is that industry ought not to be run by Civil Servants.

But need it be? Need it be, however much it is necessary to extend the field of public economic activity? Certainly not. The right structure for publicly conducted enterprise, as we have seen earlier, is that, not of the Civil Service Department, but of the Public Corporation officered by men possessing the right kinds of industrial or managerial or scientific training and experience. Neither the men at the top of the Public Corporations, nor those working under them, should be Civil Servants, as the term is now understood, or should have, as the Civil Servant now ordinarily has, any security of employment for life in a particular service. We have, then, to alter the form of our question. It should be, not Will Civil Servants run industry efficiently? but Can the State get hold of the right technicians, managers and other key workers for its socialised undertakings without turning them into persons with the qualities of Civil Servants or destroying their readiness to take risks and to regard production as an adventure in the realms of applied expertness and knowledge?

Why not—if the State devises the right instruments for this purpose, as it has done, in part, in the Public Corporations which have been already set up? There is no law of nature by whose decree public economic enterprises have to be put under the paralysing hand of those clever, uncreative persons who get into the Treasury, or to be ruled by the wish of a Chancellor of the Exchequer to balance this year's budget at all costs. The budget has to do primarily with the relation between the State's expenditure on public consumption, as distinct from public investment, and the State's revenue from taxation as distinct from borrowing for capital works. There ought to be a 'capital budget' wholly separate from the 'revenue and expenditure budget'; and the 'capital budget' ought to be the responsibility of a Minister other than the Chancellor of the Exchequer—a Minister of Economic Development and Planning, concerned primarily with capital works and with the maintenance of employment in the industries producing and extensively using capital goods. The only points at which the two budgets would interlock would be, first, that if it were decided to subsidise any industries out of the products of taxation, the current 'revenue and expenditure budget' might be called on to contribute to the cost, and secondly, that it might be decided to unbalance the 'revenue and expenditure budget' in bad times in order to contribute to the expansion of purchasing power. Such issues would necessarily be matters for the Government as a whole and would concern both the Chancellor of the Exchequer and the Minister of Economic Development; but, apart from such general issues of policy, their provinces would be clearly distinct, and would call for different qualities in the holders of these two key economic posts.

Given this dual structure, why should not skilled technicians, managers, administrators, and craftsmen work as well (or better?) for a Public Corporation attached to a State economic system as for private enterprise? There would be, indeed, no profit motive to spur them on. But is such a motive now their main incentive? Are they not mostly salaried persons, whose incomes vary, not with the amount of profit made by the enterprises they work for, but with the promotion to wider spheres of influence which comes their way if they make a success of the jobs they are in? If public enterprise meant security for life in a job, irrespective of competence, I agree that it could not be made to work well. But why should it mean this? We must make sure that it is not allowed to mean anything of the sort, and that abundant opportunity is left both for promoting good men to bigger jobs and for demoting failures.

I have tried in this book to outline the conditions of public policy which are needed in order to create and to sustain a state of 'full employment', not as an end in itself, but as the means to full production and to a high standard of living for all classes in the community. I have tried to describe the *minimum* changes in the existing economic order that will be needed in order to bring about this desirable state of affairs. I do not, however, assert that success can *necessarily* be achieved by action on this minimum scale. For one thing, nothing will succeed if there is a rooted conviction in the minds of many of those who have to take part in running it that it is bound to fail. If pessimism is uppermost in the public consciousness, infecting those who should be the leaders in every walk of society, neither the policy I have proposed in this book *nor any other* can be made to work well. If, therefore, the mood of pessimism turns out to be so deeply rooted in the minds of the key people in the economic world—business men and Trade Union leaders alike—that nothing short of a radical upset will avail to shake them out of it and set them struggling for dear life to make things work better, it may be necessary to go a great deal further than I have suggested in this book in order to produce the desired effects.

Again, if the international conditions turn out to be very adverse—with really serious barriers in the way of overseas trade and a really serious difficulty in finding means of paying for really necessary imports—the State may be driven to much more drastic measures of economic transformation than will be requisite if the great nations together are playing the expansionist game.

For, if the international conditions are adverse, not only will there be worse tendencies towards cyclical depression: there will also be much greater structural alterations to be made in the British productive system. The balance of industries will need to be different: more home agricultural production will be needed, and of different kinds; and the entire community will have to adapt itself to a lower standard of welfare than will be within its reach if world economic affairs are being governed with an approach to common sense. What I have put forward in this book is the *minimum* that will be needed for 'full employment' in Great Britain if the world in general is making 'full employment' a collective aim. It may of course be desired, on other grounds, to make much more extensive changes in the British economic and social order. But that is not what I have been discussing in this book.

INDEX