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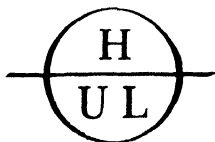
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Economic Thought and Policy

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FOREWORD

THIS book is intended to be a supplement to my *Evolution of Industry* in the same series. It deals mainly with the background of economic thought during the same period. Forty years ago, there seemed to be some finality in the conclusions of thought upon policy which gave us private enterprise, free trade, and the gold standard as definite articles of faith. One who was then a pupil of Marshall can realize how much the outlook has been changed by two influences, war, and a new economic theory. These are not unrelated, because war is the great solvent of unemployment, and the power of its 'effectual demand' sets the question of a similar power in peace. The new economics disengages the idea of effectual demand from policies in which it was implicit, and makes it a ruling concept. In a way this book is dealing continually with aspects of that idea. Economics is no longer simply demand and supply, but effectual demand for effectual supply. But I have not found that the classical economists said the things which, for the sake of an artificial contrast, are attributed to them. They did not believe in what is commonly called laissez-faire, nor in any automatic full employment under private enterprise. The difference has been only in the growing perception of the ideas which have now flowered. It will be plain that I have still some attachment to earlier economic ideas, and to the conjuncture of economic freedom which both made and was made by them.

D.H.M.

February 1949

CHAPTER I

SUPPLY AND SCARCITY

Economics is not a system of scarcities, and scarcity, absolute or relative, needs to have particular definition. Malthus foresaw the problem in relation to the limiting requisite of food supply. As the meaning of subsistence develops his problem has to be redated with reference to the maintenance of a higher standard of living. Historical progress includes the influences of discovery and invention, while the purely economic problem depends only on the latent powers of higher organization.

AN economy is by its definition a form of administration, and in industry this means that materials are used to make finished products for consumption. But the word 'economy' has come to carry with it a sense of compulsion, of having something to contend against, and in the case of industry this is taken to be the fact of scarcity. The economics of industry is then defined as the organization of scarce resources or materials for the various purposes of final consumption. The meaning of scarcity is usually taken as self-evident, and few economists have offered any definition of it. If the original resources or materials of industry are scarce, so must also be the final products. There is therefore no economics of industry except a scarcity economics.

On the other hand, many writers have contrasted the 'economics of scarcity' with the 'economics of abundance'. There has been an argument about the continuance of poverty 'in the midst of plenty'. At different times in the last century and a half, it has been held that production had reached the stage of not only

abundance, but glut, and that it was only distribution which was defective. 'During the seventeenth and eighteenth centuries,' writes Keynes, 'we fought our way out of the bondage of scarcity into the free air of abundance.'¹ The nineteenth century has been described as either the classical period of scarcity economics, or as one of imperfectly shared abundance. Carlyle spoke of our 'plethoric plenty', and one of the early Socialists had put the problem why 'where art and nature had run, as it were, a race of emulation in the prodigality of their gifts, intelligent and industrious millions should be disabled from enjoying these products of their own creation'.² The constant reference to poverty in the midst of plenty implies that scarcity has not been the dominating aspect of economics.

It seems plain that we cannot define the economics of industry as a scarcity system so as to exclude such a word as 'abundance' from its correct vocabulary. An economy is an organization of the available resources for different purposes. It is only after materials have been worked up into products that their scarcity or abundance appears, as derived from the market for these products. In themselves, they are simply available. Whether final products are scarce or abundant depends on the judgement of the consumer, who decides whether the work done for the wage which buys a quantity of product has a return which deserves one or other of these terms. The fact that products have a labour cost of production or acquisition does not alone make them always scarce. It is the purpose of economics to avoid scarcity, and there can be economics in a state of abundance. The economic aim is to use available resources so as to yield the

¹ *Essays in Persuasion*, p. 334.

² Thompson, *Distribution of Wealth*, 1822.

greatest product, and the rule for this is the equivalence of a unit of supply at the margin of each use, so that no profitable transfer can be made. When supply is thus distributed it is a truism that resources used for one purpose are not available for other purposes, but this again does not necessarily imply that they are scarce for every purpose ; that is always a question of what the consumer thinks is an adequate return for his work, and work is usually desired for its own sake. Nor does it mean that what is not used for one purpose is the cost of its use in other purposes, since in the use of resources the costs are those which are actually incurred.

Scarcity may be the result of the way in which the economics of industry is worked, but does not define economics. Some economists have given definitions of scarcity. Cassel says that 'since the wants of civilized humanity as a whole are insatiable, the means for satisfying wants are generally scarce relatively to the wants themselves'. He calls this the 'principle of scarcity', when he presumably means the fact. But unknown wants can only be related to unknown possibilities of supply, and the result of that will not always be scarcity. Cannan offers a historical definition of scarcity as existing 'when we compare the supply of one period with the supply of some other period'. But the supply might diminish for want of demand, so far as any one product is concerned; it would not then have become more scarce. Since all resources are available in definite quantities or rates of supply, it is plain that scarcity cannot be defined without reference to demand. Rarity is not the same thing as economic scarcity. To be scarce, a thing must be supplied to its market in quantities which are disposable, and this is a question of the combination into which it enters with other things in the consumption of the market.

Small quantities may be unsaleable rather than scarce. Rarity changes the market and may destroy it. It is the extrapolation or the ultra-red of scarcity. Caviare is not scarce to the general, but in another market. Wicksell, following Walras, held that 'scarcity and marginal utility are fundamentally the same thing'. This defines the demand curve for any individual, but it remains true that the use of any product distinguishes the supply as very scarce, scarce, adequate, abundant, or glut, so that more than the simple rule of demand is required. Wicksell goes further when he says that we have to consider 'the least important of the needs satisfied and the most important of the unsatisfied needs'. This introduces the elasticity of the demand as a mark of relative scarcity.

In economics, the idea of elasticity has not the same definiteness as in physical or chemical science. The same thing can have a different elasticity of demand or supply in different times, places, or conditions. It is possible only to speak of the conditions which cause the elasticity to be great or small. The first use of the word in economics was in respect of the development of human wants as a whole. 'Ils sont incessamment variables et généralement progressives, mais ils sont doués d'une élasticité, etc.' Then, in the same source, it is applied to consumption. 'La consommation n'est pas une quantité fixe et arrêtée; elle est au contraire élastique comme les besoins de l'homme, et ceux-ci n'ont de limites que les moyens de les satisfaire. Or, ces moyens satisfont d'autant plus de besoins qu'ils peuvent acheter plus de produits, etc.'¹ J. B. Say had incidentally used the phrase 'elasticity of production'.² The idea under-

¹ *Dictionnaire d'Economie Politique*, 1853, vol. 1, pp. 161, 466.

² *Treatise*, bk. 1, ch. 18.

lying the elasticity of demand was shown frequently by various writers, especially by Lauderdale, before it was named in 1878 by R. S. Moffat. 'While each producer is striving to extend his particular production . . . the permanent expansion of production of each particular commodity is limited by the elasticity of the demand for that commodity. Demand has at any time a measure of elasticity, greater or less according to the limitation or expansion of the supply.' The same author refers to the 'elasticity of production' and the 'elasticity of supply of labour'.¹ In his *Economics of Industry*, published a year later, Marshall did not use the phrase or exploit the idea. The credit for *formulating* the idea belongs to Whewell, the Master of Trinity, who expressed it in several forms as the parameter of the 'equation of supply and demand', especially the product, or xy , form of that equation.² He was aware of the problem of 'forward and backward', and of what have been more recently called 'point' and 'arc' elasticity. Marshall gave the idea graphic form in 1885, as well as algebraic definition in 1890, making no mention of Whewell. It is now a fundamental instrument of the economic calculus, and the problem of expressing it in one formula for both forward and backward movements of demand seems to have been met.³

If this idea can be used as a guide to the meaning of relative scarcity, the demand must be taken as effective and settled. The effective demand describes the class of consumers to whom the price can be said to matter. At very high prices, that class is composed of rich people,

¹ *Economy of Consumption*, pp. 122, 126, 421.

² *Transactions of the Cambridge Philosophical Society*, 1829, 1831, 1850.

³ *Review of Economic Studies*, No. 32, p. 114.

and in that market a reduction of price may glut the supply before a less rich class comes into the question; the elasticity of effective demand may be low. At moderate prices, ordinary people come into the market, and the elasticity increases, so that the supply is now felt to be more scarce, though it has physically increased. There is a greater waiting demand, until the supply increases to another stage of low elasticity. Necessaries have a low elasticity, because they have to be the relatively plentiful part of average consumption. While absolute scarcity or abundance implies the consumers' opinion on what is obtained for the income of work, this does not exclude relative scarcity in a condition of abundance; and this seems to indicate the volume of waiting consumption, or the elasticity of the demand.

There must be room in economics for the concept of plenty and abundance, and if we define it as an organized scarcity, or an organization of scarce resources, resulting in scarce products, we do not leave room either for legitimate descriptions of the results of organized supply, or for the features of different stages of the evolution of industry. Scarcity, abundance, and glut are all proper descriptions of certain analytical or historical conditions.

The problem which was set for economic thought by Malthus was, how it was possible for a growing population to ensure that the reward of work could continue to deserve to be described as abundant, for the people as a whole, of a nation or of the world. He perceived the economic problem in its most general terms and its largest range. The economic system at any time is made up of a complexity of arrangements for making the available resources and primary materials into goods for consumption. The complexity of organization

may be so great as to create a science of its own, and to have an interest of its own as a form of human activity. But however well we handle the primary resources, however quickly we move them about, however skilful labour becomes in saving time, the basic question remains of the amount which goes into the system of production, and which limits the amount of consumption. Nor does it matter whether the available resources are passed on through large-scale units of production or smaller ones. The question is, what is available to pass through the channels of supply, whether these channels are wide or narrow. The complexity of industrial arrangements disguises what to Malthus was a problem of polarity—the poles of the system being population and natural resources. All the interactions of the system of supply take place between these poles. Thus Malthus wrote the economic problem down to its simplest terms. He stated it in the skeleton terms of demand and supply as quantities independent of manipulation. The nineteenth century developed the study of industrial organization as an activity which, between the poles of the problem, somehow overcame the problem of the relative quantities of population and resources. This is for later study. But, since Malthus' time, economic science was also beset by the idea of limiting conditions which he splashed on his large canvas, and it has granted the insistence and permanence of his conditions. But, because of historical events which he could not foresee, which have changed the conditions of supply by discovery and invention, it has constantly redated his problem, so as to relate it to the continuance of a changed standard of living.

The problem of scarcity was set by Malthus in respect of two 'constants' and two ratios. His first constant was

the 'passion between the sexes' or the 'power of population'. 'The passion between the sexes has appeared in every age to be so nearly the same that it may always be considered, in algebraic language, as a given quantity.' If this power of population were not what he calls a constant, if it were related to the standard of living, his problem might not arise; if people had less desire for children when the standard of living increased, or if that desire declined faster than the standard of living declined, then the power of population would have been one of the social elasticities, carrying with it the possibility of a maintained standard of living. But Malthus vaguely defined it as a constant, with no functional dependence on the standard of living; it gave the economic problem of the relief of scarcity an irrational factor to contend with. He did not say at what figure of fertility this power was constant. His other constant was what he called the 'walls of the room', or the limit on the productivity of any area of land. 'You are limited by the walls of the room', he said, 'even when you are not touching them.' An 'indefinite' increase in productivity is possible with an increasing population and labour supply, but indefinite is not infinite, and the productivity is at a constantly diminishing rate.

This problem of the diminishing return of any area of land to increased labour could be posed in respect of any sort of supply, since all supplies are derived from the resources of land. Malthus made it particularly a question of food supply or subsistence, as being the fundamental or limiting requisite of the standard of living. He was justified in this, because agriculture is the greatest user of the area of land. Even in Britain, which does not produce more than half of its own food, 80 per cent of the land area is agricultural, and this is

chiefly for food. Mining and transport are not, by comparison, great users of land. And, among agricultural products, food has an obvious priority in the general question of abundance or scarcity. This led Malthus to state the economic problem in terms of 'subsistence', as others, notably Bentham and Steuart, had done before him. Of course, at his time, the variety of consumable goods was far less than it became later, and subsistence was the obvious criterion of scarcity or abundance.

Between his two constants, Malthus placed the operation of two ratios. Population has the power to increase in a geometrical ratio, since the impulse applies to the increase, as well as to the previous quantity, and does not decline. But the 'land' cannot supply its materials without exhaustion, so that even an increased labour supply cannot obtain supplies at its own rate of increase. He implies the law of diminishing return. Population has therefore a power 'of superior order' of increase to the powers of supply; at the most, he allowed the power of land, in respect of subsistence, to increase in an arithmetical ratio. These ratios of Malthus are not now important; it would be sufficient that one of them should be greater than the other, and this is what the law of diminishing return states. There is always some geometrical ratio which will be less than any arithmetical ratio over a given time. Malthus had therefore to state a period of time for the doubling of both supplies and population, and he gave twenty-five years as an initial period when this might be possible. Thereafter, the stronger ratio would overcome the weaker, unless a new influence called 'restraint' came into play to lessen the pressure on supplies. Failing restraint, there would be scarcity, starvation and misery. But restraint is itself a sacrifice, a form of misery. The economic problem

could not therefore be solved in terms of both welfare and happiness. To avert scarcity from themselves, nations would go to war, the extreme form of misery.

Malthus developed, with great historical and social insight, an argument of which the general nature was obvious, so that economic science during the nineteenth century was greatly concerned with the population question. It beset especially the economic outlook of Mill. And a Malthusian strain has persisted up to the present time. It is impossible to deny that the relation of population to land resources is an envelope, or general condition, of economic argument, and that food supply is greedy of the area of habitable land, and that scarcity of food is not compensated by abundance of other supplies which are users of less land.

Answers to Malthus are qualifications of his argument. When he said that the passion between the sexes was 'a given quantity', he spoke vaguely. It is constant, but not therefore a constant. It can be constant and also functional, depending on the content of subsistence, and on this ground Henry George and others insisted that 'man developes'. The 'tendency' of population therefore became historical instead of physical or physiological. As people get better off, they have more things to think about than sexual indulgence. This is not restraint, as a form of misery, but education, civilization, and interest. Man was not 'made to mourn' just because he cannot have eight or ten children. This reply to Malthus took one form of misery out of his argument, without settling the opposition of his ratios, as affecting scarcity over any period.

Another answer to Malthus was given by Paley, Rickards, Henry George, and others, when they said

that the 'animalism' of unrestricted human increase was offset by a similar law of increase in nature. They instanced the tremendous rate at which some of the lower types of life increased, and suggested that the animals used for human food, as well as the grains, had as great powers of multiplication as mankind. 'We can always command numbers,' said Paley. But there are definite multipliers of yield, on any quality of land, for any sort of stock or grain, and it is the amount of land they need that still limits their total yield. For instance, it takes between 3 and 4 acres of land to graze and feed a head of cattle under average conditions. The animalism of unrestricted nature does not offer a remedy, because the walls of the room limit it, and this argument only shifted the problem from its general statement to its particular application.

A historical answer to Malthus would be a question of his starting point. If we start in England at 1400, then the period 1800 to 1825 would be the seventeenth of his twenty-five-year divisions, and population could only increase by one sixteenth; if we start at 1700, the same period would be the fifth and population could increase by a quarter. This shows that his argument has to be taken in a general form, and redated according to changes in discovery of resources, and to historical accidents. What he calls 'easy conditions' may thus periodically exist but, whatever the historical position at any time, scarcity threatens it unless by restraint the two powers of land and human fertility are kept from conflict.

Then came the answer of economic science which, while realising the force of Malthus' problem of quantities, and accepting the case for restraint, made out a case for another influence on the standard of living which

was not a form of misery, namely, the 'increasing returns' of organization. The statement that, by the way we handle supplies which become less available per head of the people, we can still have abundance, is obviously sensational. This action of increasing returns has been disguised in the nineteenth century, because it was accompanied by great changes in discovery and invention; so much so that some authors regard it as only an historical fact, a name for the result of all historical influences. But, standing by itself, the power is attributed to it of overcoming diminishing returns, by the devices of the economics of industry.

As a matter of history, we cannot separate the results of discovery, invention, and organization from each other. In a period when the return to ordinary labour is considered to deserve to be called abundant, these three influences have been mixed. We can endeavour to get an answer to the historical question, how much of progress has been due to each of these causes. If, as some writers hold, there is no device for relieving scarcity by the mere manipulation of supplies which diminish per unit of work, then periods of abundance are due to the historical accidents of discovery or invention, and the question of progress is one of the elasticities of these forces.

Discovery has an extensive and an intensive form. As regards the first of these, the exploration of the land area of the world has an absolute limit of space. For economics, discovery means effective occupation and exploitation, not merely the work of pioneers. Its force can be considered by reference to the limiting requisite of food supply. The population of the world has doubled in the last hundred years, and is now about

2,200 millions. But this is not a large figure against the acreage of the land area of the world, which is nearly 36,000 millions. We cannot get any conclusions on the world's poverty or scarcity out of a comparison of different and arbitrary units; we could take the world's families, instead of its heads, and its miles instead of its acres. There are 16 acres per head, or perhaps 60 acres per family. The sparsity of the world's population, and the figures of undeveloped areas, have led some authors to regard diminishing return as, for the immediate future, a myth. But, for economics, discovery is effective occupation, and this alters the figures greatly. There has to be a coincidence of conditions of climate for both human beings and physical resources. The latter is the more critical condition. We cannot increase at all the resources which are of the nature of deposits, while over 40 per cent of the land area is either too hot or too cold for crops. When all conditions of heat, moisture, topography, and soil are allowed for, it seems that at present only about 7 per cent of the land area is suited to agricultural crops and less than 5 per cent to food crops.¹ Extensive discovery played a large part in the nineteenth century, but its elasticity is now not very great. Possible increases in the crop area are offset by exhaustion, through erosion, of the fertility of existing areas which were overcropped for many decades. Malthus is supposed not to have properly allowed for extensive discovery, and hence the redating from time to time of his problem. On the other hand, intensive discovery, of the potentialities of discovered land, has an unknown elasticity, as is shown by the history of radium and uranium. Intensive discovery has not the same application to crops as to minerals and other deposits. The grains,

¹ F. A. Pearson and F. A. Harper: *The World's Hunger*, 1945.

animals, and other agricultural supplies have not any great reserve of discovery. The mineral resources and powers which offer most scope to discovery may enormously increase the speed and efficiency with which other material supplies can be processed, but the standard of human consumption depends on the other things which enter into process. Malthus admitted that his argument could apply to other things than food supply or 'subsistence', while perceiving the essential difference between what we live with or by, and what we live on.

Scarcity can obviously be alleviated by discovery, but the economic problem touches more closely when that factor is put aside, and we have to consider the future when extensive discovery is used up. The strict economic problem is also taken to exclude the factor of invention, in the sense of technical discovery.

The Malthusian problem is one of the relation of human demands as a whole, whether of the world or of a nation, to the original powers of physical supply. The latter are chiefly laws of physics and different branches of chemistry. The foreground of the economic question is filled by numerous arrangements, national, international, and industrial, for the purpose of arranging the methods and direction of supply. The complexity of these arrangements disguises the conditions on which all supplies are finally available, until some exceptional event, like war or drought, reveals the dependence of all organization and employment on what is available to organize and work upon. The problem is further disguised by the different conditions of different countries. In this country, which has to import most of its materials, the amount of output and employment

depends on the terms of trade on which we can obtain the materials to work on. For the world as a whole, these interactions are cut out, and the wars have made plain the entire dependence of population on its primary production. It is not labour that is scarce, or time. When we speak of scarcity of labour, that is a question of its distribution; but more population, or longer hours of work, are demand on resources as well as supplies. Population is not scarce in relation to itself. Nor is time a scarce factor. The phrase that 'there are only twenty-four hours in the day' has no clear meaning for economics. In the measurement of the rate of output against the rate of input, the time is eliminated. Time is a condition, not a factor.

Malthus thought that the evolution of industry was assisted by the pressure on supplies of the standard of subsistence; but for this, he said, mankind would never have emerged from the savage state. A century later, Marshall stated the contrary view that it was new activities which created new wants, not the other way round. Wants and activities interact. Backward nations have so remained for long periods of time, while developed nations have had the greatest elasticity of development. The view that a strong pressure of demand on supply was a favourable condition of both employment and evolution led Malthus to hold that there should be a number of unproductive consumers, like the holders of the national debt, in order to prevent over-supply and glut and depression of industry by the force of a strong 'effectual demand'. This was one of a number of absurd arguments in favour of national debts about his time, and was obviously inconsistent with his theory that population would always increase so as to consume additional subsistence. Say replied that the desirable

condition was a pressure of supply on demand. The 'pressure' idea was taken out of the argument by the concept of equilibrium, which creates supply for demand, and demand for supply, if the whole income of a nation is spent as it is earned. This equilibrium may be one of either scarcity or abundance, as a matter of judgement on the intensity and interest of work in relation to its results.

The Malthusian argument caused the phrase 'demand and supply' to be used with a sense of criticism or impatience of economic thought, because it seemed to imply that hard conditions were unavoidable. The economic parrot would, it was said, always answer 'demand and supply' to everything. But the moral parrot would say 'right and wrong', or the legal parrot 'law and order', or the logical parrot 'true and false'. There could also be military, theological, political and other such birds. Every field of study is defined by some fundamental concept, and those to whom it is not readily clear what is meant by the study of a particular aspect of human activity cannot have it easily explained to them. The argument of Malthus simply short-circuited the vast complications of the economic system, and brought it to its final terms. As the world in the twentieth century is finding out, these terms remain final, whatever arrangements are made for directing and distributing supplies. In conjunction with 'demand and supply' went the concept of 'economic man', as if there were not also military, ecclesiastical, academic, political, and scientific man. One would have supposed that military man offered the most 'dismal' study, but Adam Smith held, long before Ruskin, that 'the art of war is the noblest of all the arts', and this is the extreme instance in which interest in an organization overcomes

interest in its products. While there are all these different 'men', there has always been a special isolation of economic man and his motives. The hardness of his system and motives is related to that of the ultimate facts which Malthus perceived under simple conditions, and which were always ready to obtrude under more complex ones. At a late stage, his law could be elaborated by Stamp in the statement that 'the economic life is a complex reaction between a physical world, obeying the laws of physics and chemistry, and living organisms obeying more elusive biological and physiological principles, the whole relationship being worked upon by individual and mass psychological and spiritual forces'.¹

The strict economic reply to Malthus has been given in the theory of organization. It is by this means alone that, in given conditions of invention and discovery, the danger of scarcity is to be averted, in spite of the law of diminishing returns; and this is the argument which has been referred to above as sensational. Organization is the way we handle supplies, and can it from time to time solve for an increasing population the problem of the supplies themselves?

The separation of industrial organization from technical invention is very difficult to make. It is often because of the nature of a technical invention that organization, for the use of such inventions, takes the form it does. On the other hand, it is claimed to be one of the economies of organization that it leads to a greater provision of research by large businesses, so that it is closely bound up with invention. More than this, one of the economies of organization, the division of labour,

¹ *Economic Factors of Modern Life*, p. 185.

is credited with the invention of machinery, when manual processes have become regular and repetitive. And, at the other end of the process, large-scale business management is credited with the power and readiness to use the most up-to-date machinery. But, while these two influences of invention and organization are so closely related in practice, the statement of the economic problem, in reply to Malthus, insists on their separate consideration. This suggests that invention is unreliable or exhaustible, and that for the future, whenever we redate the Malthusian ratios, we have to rely on the steady influence of something we can always command, the organization of industry.

We invent products, processes, and instruments. In that order, they depend on each other. A new product, like the bicycle or the motor-car, implies a new process with new instruments. By itself, the new product may or may not economize national resources. It contributes to the variety of national consumption, but it may divert materials and labour according to the standard of wants, or market demand, and not according to the standard of needs, especially if there are great differences in purchasing power. The new process depends on the nature of the new instrument or equipment of production. The net gain depends on whether the new instrument, being itself a consumer of materials and labour, makes less demand on these resources in order to supply the same amount of the product which it completes. This is technique, and the field of its application is the instrumental side of industry. It may act in any or all of a number of ways, by making new instruments which either require less material for their own construction without loss of their power to process other material, or require the co-operation of less labour for a given process

of production, or use less of the fuels and auxiliaries of production for a given process, or lose less of the processed materials in course of the process. In general, whether the primary impact of invention is on time, skill, or materials, it creates some surplus of both labour and materials, which it is for organization to combine with each other for a new product or the increase of an old one. This is a decrease of scarcity, since no increase of the population needs to have taken place. A purely labour-saving invention means that more labour can be applied to existing resources of land, and the return will not increase in the same proportion, but it is sufficient that there shall be any increase at all for the same population. And obviously there is some increase of population which will be within the efficiency of an invention to increase supply.

Invention, therefore, like discovery, can give what is called increasing return, and help to avert scarcity. But the law of increasing return explicitly excludes both invention and discovery. It is stated in terms of the power of organization alone. 'An increase of labour and capital,' writes Marshall, 'leads generally to improved organization, which increases the efficiency of labour and capital,' and this is his definition of the 'law of increasing return'. Organizers will, in his analysis, use the best inventions, and may make some of them; the representative business 'has access' to the technical economies of any period. But, when we are considering the long tendencies of supply, 'we exclude from view any economies that may result from substantive new inventions' and include only those which 'arise naturally out of adaptations of existing ideas'. For 'normal' conditions there must be 'no new invention to disturb the supply'.

The empirical answer to Malthus is that he could not foresee the results of discovery and invention, and the empirical question of redating his problem is whether these forces are tending to be spent, so that the future question of scarcity or abundance is more urgent. His problem is redated when we ask whether a new standard of living can be continued against the force of population. If we place this burden on the powers of organization alone, these must give increasing returns in an increasing degree, as long as population increases. It is for that reason that the strict scientific answer to Malthus, the power of organization, appears to be paradoxical or sensational, because it asks so much and seems to be only the handling of available supplies.

The theory of organization does, however, show results similar to those of invention, at a more regular pace. In every industry that is highly organized, the economy of supply is a question of its staple, its equipment, and its auxiliaries. The staple is the material which passes through its process into the form of a final product. An increased amount of final product requires an increased amount of the staple. But it does not require an increased amount of the equipment or the auxiliaries. In a larger scale of production, which is the main feature of higher organization, the layout may, by mere concentration, require less than twice the material of machinery and building, as well as of fuels, in order to double the output of the establishment. This is not technique, or new powers of machinery, but simply economy of size. But materials which are equipment and auxiliaries for one industry are needed for other industries, either as equipment and auxiliaries, or even as staples. The internal economy of organization thus creates what are

called external economies, which become internal elsewhere. In the iron industry, the material of equipment is also that of its own staple, so that it gains twice over by the economy of its organization. Other industries gain once only, by the saving for them of the materials of equipment and auxiliaries. Agriculture is a small user of steel, to the extent of only 4 per cent of the supply in America, and is only slightly helped by the general sharing of supplies which higher organization makes possible over the whole field.

But, while invention has an indefinite and irregular power to save material supplies by technique, organization has much closer limits. The scale of production is thought, by both theoretical and practical accounts, to reach an economic limit of the unit of management, which is its critical feature. In the second place, it has its least important application to agricultural supplies, and an economy which greatly increases the products of its other industries will have scarcity unless food supply is increased also. Of course, invention shares this latter handicap. Food is a staple, which is not saved out of economies of invention or organization in other industries. It depends mainly on the internal economies of handling its own materials, so that the largest possible proportion of what enters the process passes through into the product.

There is one mixed result of invention and organization which has eased the pressure on some material supplies. Some staples, having been processed, pass into an entirely final consumption; this is especially the case with food supplies. But others pass through many stages of consumption, being durable articles which are not destroyed when they have completed their first use.

They are then used again, and have several lives, and are substitutes for new supplies, so as to take pressure off the sources of these supplies. Once they are above ground, the supplies of metals are only slowly destroyed, so that after use in one way they can still be adapted to use in other ways. This 'secondary' production has become an important factor in the economy of industry. The U.S. National Resources Board states that 'while in 1910-14 secondary copper and lead were each equal to 14 per cent of mine production, by 1924-8 the proportion had increased to 38 and 40 per cent. In 1933, the production of secondary copper reached the astonishing figure of 133 per cent of the mines' output'. And in this country it is stated that 'whereas in 1939 the average proportion of the charge for every ton of steel produced was 10.9 cwt. of pig iron and 11.2 cwt. of scrap, in 1944 it was 9.5 cwt. of pig iron and 12.14 cwt. of scrap'. (*The Times*, 25 Oct. 1945.) Reclaimed or regenerated rubber reaches figures of from 40 to 60 per cent in some branches of the motor industry.¹ Woollens are regenerated as shoddy, and cottons as paper. The point here is, that the new product does not require a new application to 'land'. This alleviation of pressure on the land is to be taken net in so far as it substitutes a second cost of processing for the cost of obtaining new supplies, but it is gross in relation to the supplies themselves. In respect of agricultural supplies, this kind of economy does not have much, if any, application. It is true that animal and vegetable manures are applied to the soil, but this aspect of farming technique is quite different from the re-fabrication of the products themselves. When shoddy from the textile industries, or basic slag from the iron

¹ Haynes: *The Chemical Age*, 1946, p. 138. Possony: *Tomorrow's War*, 1938, p. 164.

industry, is used as manure for the production of crops, that is an ordinary incident of methods of production, but it is not a relief of land from the pressure on food supplies. Just as it is out of the main current of inventiveness, so is agriculture also out of the economy of accumulated stocks, and therefore of an offset to diminishing returns which is important elsewhere.

In connection with the multiple use of accumulated stocks is the question of the rate of exploitation of natural resources during the last century. A problem arose of the 'conservation of natural resources', which had begun to be a feature of world planning. 'Until recently,' says the U.S. National Resources Board, 'consumption (of metals and fuels) has increased like a sum at compound interest, so that in the last thirty years we have used more coal, oil, iron, and copper than in our entire previous history. The problem of conservation is not to prepare for a day centuries hence when all the fuel and metal shall be gone, but to minimize the readjustment to a stage of increasing cost which in the older lands has already arrived, and in the United States is only a matter of time.' The same argument was used in 1865 by Jevons in relation to British supplies of coal. It is suggested that the nineteenth century may have got its historical increasing returns on conditions which cannot be maintained; that it 'delivered the goods' by a false increasing return which concealed the costs of depreciation. Evidence has been given that agriculture suffered especially by the pace of cropping which the growth of world population made necessary, which has thrown much valuable land out of use.¹ Duty to posterity is a difficult question, since it includes the unknowns of future inventiveness, against the known urgency of

¹ G. V. Jacks and R. O. Whyte: *The Rape of the Earth*, 1939.

present demands; and a high tempo of industry in any generation itself contributes to the inventiveness which will be passed on. If a policy of conservation is now thought to be necessary, this is a further aspect of diminishing returns. If the increase in the standard of life in the last century was artificially raised by the rate of exploitation, it is this costly standard which it is now sought to maintain, so that Malthus's problem is extended to more than what he called subsistence. When we say that we have to redate that problem, we mean that we are raising our claim upon future supplies, upon the intensive discovery, the invention, and the organization on which they depend, and against the undoubted constant of total area.

In the nineteenth century, the result of discovery, invention, and organization was, that the average wealth of this country increased four times with a fourfold increase of population. It has been said that in this period capitalism 'produced the goods', but the extension of the exploitable areas of supply has to be remembered. The statistical results of the increase of average wealth also claim to show that this increase was shared by all classes of the people in about the same degree. There was a stability in the distribution of income which showed itself by three indices; wages were 40 per cent of the national income; the average wage was half the average income; and therefore wage-earners were about four-fifths of income-earners. It is only quite recently that these ratios have slightly varied, and it is still usual for income statisticians to use Pareto's law of stable distribution as a verification of income distribution. But, by the test of the limiting requisite of food supply, these figures of progress offer some difficulties.

At the end of the century, the inquiries of Booth, Rowntree, and others, based on subsistence, gave the conclusion that about one-third of the people lived below a 'poverty line'. For the working-class alone, it was over 40 per cent by Rowntree's estimate. This is difficult to square with a fourfold increase in average wealth, which was equally shared by all classes during the century. For what is it to be four times as badly off as the poverty line of 1900? How can the conditions of the working-class in Malthus' time be conceived? Yet it was in the early years of the century that the population grew fastest.

Progress has a regressive interpretation. It is not the only test of welfare. There would have been less progress, but more welfare, if the early conditions had been more equal to the later. So far as an optimum condition is created in any sphere, progress is stopped there, and shifted to other spheres. There cannot be anything better in its own sphere than full employment. A verdict on the progress of any period may be in fact a retrospective censure. This has happened in respect of the nineteenth century. There has to be 'historical sense' in the interpretation, and it has to be applied to both avoidable and unavoidable conditions, both human and physical. It is the interpretation itself which is the difficult feature of the statistics of the progress of welfare.

The conclusions reached, in quite recent years, by research into the standard of living, show that a fundamental scarcity has been a continuous feature of the economy. These conclusions are based on a standard of needs, not on a standard of market demand. 'There has never been enough food for the health of all people,' was the opinion of the Food and Agricultural Organization in 1943. 'It has been estimated,' said the

Agricultural Department of the U.S.A. in 1941, 'that 45 millions of our people are living below the poverty danger-line.' In the opinion of Sir John Orr, 'a diet completely adequate to health according to modern standards is (1936) reached only at an income level above that of 50 per cent of the population'.¹ Many other inquiries give similar results, and insist on the need for greater production of food. After a four or fivefold increase in welfare since Malthus' time, these results continue the paradox of the earlier poverty inquiries.

The difficulty is resolved by the fact that a change in general purchasing power increases the variety of consumption and the influence of taste on the objects of expenditure. In respect of food, this results in a greater demand for animal as against plant or grain products. Rich countries spend a larger proportion of their income on animal products. In proportion to their subsistence value, in what are called calories, these products are very expensive, as much as eight or ten times as expensive as the grains which are the staples of human food. About 40 per cent of grains are fed to animals, who use up their subsistence value in keeping themselves alive, and yield in meat only a small percentage of the value of grains directly consumed by human beings. Animals are also great users of space for their own support. Hence animal products are so dear that only rich nations can afford to use much of them. Only 9 per cent of the weight of consumption is animal food over the world, but in North America it is 25 per cent, and in Asia only 3 per cent. This difference of the present time conforms to the historical difference in the consumption of any one country over a period of time. The simpler standard

¹ *Food, Health, and Income*, 1936.

of consumption had a greater subsistence value per unit of weight than the later and more varied standard. The standard of needs did not and could not change as much as the standard of wants. It has been calculated by Middleton that the average Englishman had only 9 per cent more real value of consumption in 1914 than in the thirties of last century.¹

While it is thus possible to even out the figures of progress, it remains, by reference to the recent figures, that food supply has always been scarce by the standard of needs, the increase of population having fully kept pace with that of the available area of supply. The supply problem of the future is the development of that area by new methods of intensiveness, or by intensive discovery. The 7 per cent of the land area which is now estimated to be available for crops under present methods may be extended by discoveries which remove or lessen the restrictions which climate imposes either on produce or on human labour. It is said that the discovery in 1948 of the anti-pest drug Antrocyde may make about 4½ million square miles of central Africa available for stock farming, and this alone is over 7 per cent of the land area; it would release for grain as much as could be unconditionally diverted to that purpose in the whole of the United States, or in four times the area of the Argentine. It is the very smallness of the proportion of the land area now available for food supply which enables some non-Malthusians to minimize the fear of future scarcity, while others have an indefinitely extensive belief in the possibilities of planned science. 'The communist answer is to laugh at the delusion that there is any such thing as a Law of Diminishing Returns. . . . Even our existing knowledge would enable us to multiply

¹ *Food Production in War*, 1923, p. 96.

many times the amount of foodstuffs that the agriculturists at present produce. To the communist it seems that it requires only scientific planning to demonstrate to the most sceptical practical man that the Law of Diminishing Returns is, with the technical science of the twentieth century, no better than an economic myth. The world is living in fact under a Law of Increasing Returns likely to endure until a date too far remote to be taken into account in twentieth century planning.¹ Whatever the beliefs for the future may be, it was invention and extensive discovery which chiefly mattered from Malthus until now, and these have done their service. Without regard to political views, we cannot be more than hopeful about intensive discovery and the counter-agents of climate.

The other, or demand, side of the question is population policy. Keynes took this to be one of the clear cases of the 'end of laissez-faire', one of 'these functions which fall outside the sphere of the individual' or 'decisions which are made by *no one* if the State does not make them'. 'The time has already come when each country needs a considered national policy about what size of population is most expedient. And, having settled this policy, we must take steps to carry it into operation.'² It is not easy to define a population policy. So far as quality is concerned, this results from educational and public health policy, and is not a separate thing. The distribution of population is also mainly dependent on social and industrial policies of health and employment. A strict population policy is, as Keynes defines it, one of the quantity of population in relation to economic

¹ Webb: *Soviet Communism*, 1936, pp. 683-4.

² *The End of Laissez-faire*, pp. 46-8.

conditions and resources. An effective policy is not one of advice and warning, such as Malthus and Mill proposed; nor the sort of sexual communism which Plato wanted for his elect. Policy depends on the use of some instrument, which can be adjusted so as either to restrain or encourage; it must be able to act either way. But that is the difficulty. It is easier to think of methods of encouraging the growth of population than of methods of restriction. It might even be considered a fundamental freedom of healthy married persons to have as many children as they could maintain. In that case, population policy could only act one way; it would be different from, for example, tariff policy. The chief instruments of population policy are marriage or family allowances, and these are not likely to be reduced once they have been started. It is also uncertain how they will act. When family allowances were proposed for this country in 1924, it was argued, with statistical support, that their substantial effect would be restrictive, because of their influence on the standard of living of a large class of working people.¹ But the opposite conclusion was substituted later, when that conclusion was desired through the discovery that population might be tending to decrease while it was still actually increasing. Yet the allowances would have been paid on other grounds, whatever view was held about population. For military reasons, most countries wish to have large populations, and the modern doctrine of full employment is unconditional as regards the size of population. A population policy has to make terms with a vested opinion in favour of private freedom of parenthood. It is not plain what is the nature of the 'decisions' which Keynes would have wished to enforce. In that case, the greater influences

¹ E. Rathbone: *The Disinherited Family*, 1924, p. 247.

in defeating or postponing scarcity have to come from the side of supply. That is the serious aspect of the question, because of the undoubted constant of the total land area, and because agriculture is not in the main current of inventiveness.

CHAPTER 2

THE REPRESENTATION OF SUPPLY

The avoidance of scarcity by organization is impeded if large-scale production itself involves a restrictive element. This is suggested by the theory of imperfect competition. It raises the question of the interpretation of the 'supply curve' as the locus of a cost. The issue is between the results of pure analysis and the psychology of rival producers, with some reference also to the history of monopolistic competition.

THIS chapter discusses the manner in which the avoidance of scarcity, by the force of the organization of production, is represented. That is a question of the form of what is called the 'supply curve' of any product.

This curve is meant to show the movement, or to be the locus of, the cost of supply. The real cost is the amount of work or effort that is needed for a unit of product. But if the time-cost of labour is given, and if organization increases the product for the same time, then the movement of the money-cost or price can be taken to show whether the economies of organization are overcoming the tendency of original material supplies to become less available. Then the supply curve shows the movement of a price, and increasing returns become decreasing prices.

If the supply were monopolized, the supply curve would show the movement of monopoly price as the market increased; if not, it would show the movement of some degree of competitive price. Between complete monopoly and perfect competition there is the case of

production by large producers, and this is the very case in which the economies of supply are expected to be obtained and handed on to the consumer. But it is now debated whether this will happen, and which of two assumptions is the right one; whether the competition between large producers is so strong as to compel them to sell at their lowest cost, or whether their size, and individual influence on the market, is such as to make their competition 'monopolistic', in which case the supply curve does not show the result of the possible economies of organization. In the latter case, the economy of organization partially defeats itself, and its main instrument, the scale of production, has a restrictive as well as an expansive tendency. This is practically important, because it suggests that there is a point at which the economy of organization is in danger of turning against the interest of the consumer. The question involved is partly one of analysis and partly one of the psychology of enterprise. In the argument of Marshall, the assumption is made that the full economy of large-scale enterprise reaches the consumer, and that the supply curve is the locus of a minimum cost; but later analysis amends this result, so that the supply curve shows only the movement of a cost above the minimum, or an economy of running short of capacity. It is this antithesis which has to be considered.

The supply price of anything is a price which varies with the quantity offered on the market. The quantity offered is the joint product of a number of producers, who differ from each other in their conditions of production. But between them they supply at any time a certain quantity per month or year; the supply is a *rate* of production. The price obtained for a unit of the

supply depends on the demand. If the rate of production is to be maintained, the demand price must cover a cost of production which is in some way a standard for all the producers. If the demand price covers this standard cost, the demand is said to be 'effectual'; that is to say, it ensures the continuance of the rate of supply.

When we say that there is a supply price for a certain rate of production, allowance is made for the irregularities which occur in any market for short times, because the supply of a number of separate producers cannot be adjusted to an exact amount. The supply price is the price of the output around which these irregularities take place. These irregularities are a different thing from what are called 'fluctuations', because fluctuation implies changes in the *conditions* of either demand or supply, whereas irregularities do not. Irregularities are inevitable in a complex system of production, but they do not tend to displace the standard price or cost, to which the market tends to return. Fluctuations displace the standard price or cost for a time, which is called a 'short period', in which the conditions of demand or supply have changed. Both irregularities and fluctuations take place around what is regarded as 'normal', but the fluctuations are larger and slower movements about what is normal. Normal means that no permanent change in the market can be reckoned on, so that the producers do not change their equipment or investment.

A change in the size of the market, by increase of population, or shifts of demand from one thing to another, or increase of foreign demand, means that there is a new rate of output, and a new standard price and cost. The new standard, about which irregularities

and fluctuations will again take place, may be either higher or lower than the old one. This depends on the elasticity of the supply, and on the manner in which the new rate of production is *organized*. The sources of supply consist finally in natural deposits, growths, or powers, which are exhaustible, so that it becomes more costly in labour to obtain extra products from them; but, on the other hand, it may be possible to *economize* the supplies, so that less of them are used up in the production of a unit of final product. This is the part played by *organization*. It may or may not be possible for the economies of organization to overcome the exhaustion of original supplies. Therefore, the standard supply price or cost may either increase or diminish when the market is permanently changed. Production is said to be *adjusted* to a change of the market when a new standard cost is covered by a new 'effectual' demand price. Then the new rate of output is established.

A 'supply curve' shows what is the standard cost at which a new rate of output can be maintained by all the producers between them. Between them, they make the standard cost, and it reacts on each of them. It may not be the exact cost of any of them, though some of them will have more influence on it than others; it is a matter of further discussion whether what may be called the 'price-determining cost' is the specific cost of any particular producers. It is sufficient at present to say that, when a supply curve is drawn, the standard cost and price so react on all the producers that the rate of supply corresponding to that price and cost is maintained.

When we draw a supply curve in this way, we are dealing with economic analysis, not with history. If there are new inventions, or new discoveries of sources

of supply, that is history. If new sources of supply are discovered, a fall in the supply price of products offers no problem. The economic problem is whether the demand of a larger market can be supplied at rising or falling unit costs by the force of *economy* alone, that is to say, by the way we use our supplies. It may seem strange to isolate invention and discovery in this way: and some changes in organization are hard to distinguish from inventions, but of course there is an economic problem of the right use of inventions and discoveries. Of course, too, if the increase of the market is the result of a growth of population, there is more labour as well as more demand. It is, however, just the economic problem whether this increase in the supply of labour can meet its own increased demand at rising or falling costs and prices without the help of inventions or discoveries. There is an elasticity of population or demand, an elasticity of organization, and an elasticity of discovery and invention. These three elasticities constitute the *historical* problem of the standard of life. The economical problem is one of what *economy* can do, that is, of how the available resources can be used to their fullest advantage. The answer is shown in the 'supply curve' of costs and prices, drawn in accordance with an argument on the possibilities of organization. In economics, we have to argue *to* diagrams more than *from* them; the diagrams depend on the argument. The diagrams may fail when the argument does not. On the other hand, a diagram may show how far an argument is consistent, or requires revision. Again, argument may agree with diagram on specific points of the latter, while the change from one such point to another may be good in argument but fail on the diagram. We may only be able to show broken arcs of the supply curve, corresponding to

ranges of change in supply, and not to a continuity of change. But this may be sufficient for the illustrative use of a diagram.

We have now to consider in detail this problem of a standard price and cost in relation to the maintained output of a group of independent producers, who are in competition with each other. This group does not consist of always the same people. While the whole output is maintained at the standard price, some of that group increase and others diminish their supply; some leave the field while others enter it. This is because of the reaction of the standard price upon their different efficiencies. In economics, inefficiency does not mean defect of skill. It means inability to cover full costs at the standard price. A new business is likely for a time to be less efficient than an older one, because it has not yet obtained a business connection or custom. Any business may find that its location places it at a disadvantage by a change in conditions of transport, or by a local shift of demand which affects its buying or selling prices. For the same reason, others may gain in their efficiency, that is, their power to meet the effectual demand price. Of course, there may also be the sheer inefficiency of bad management, or failure to use properly the internal or external economics that are available. The evidence of many public inquiries into industrial conditions shows how these changes have taken place. The less efficient producers at any time can supply at the standard cost only at low profit or a loss, but at another time they move into a better position in the group, and are able to cover their full costs. The statistics of industries show how at any one time there is wide variation in the profits made by various producers, according as they are at that time large or small, young

or old, better or worse located, better or worse placed in relation to labour, better or worse organized. But they are all subject to what may be called the 'price-determining' cost, at which between them they maintain the supply, while the young grow old, the small grow large, the locations get better or worse, the new enter, and some leave the field. This is the economic conception of a 'stationary state', which covers all these changes among the producers behind the front of an output maintained by them all.

We have now to ask how this standard cost, at which all must sell, even if their industrial costs vary from it, is determined. Is it the cost of some or any producers who have what is called 'price-leadership'; or is it some kind of average, which may not be the same as the actual cost of anyone at all? In any case, we come up against a number of economic terms which have to be related to the cost. They are the words average, marginal, minimum, and representative (or typical).

We assume a competitive market; the producers have not in any way combined or agreed with each other. If the producers are very numerous, so that none of them can by himself affect the price, because his output is a small part of the whole, this has been called 'perfect' competition. This is a curious definition, because price is the usual instrument of competition, by which a producer attracts trade from others to himself. On the other hand, competition has been defined as imperfect when some producers are large enough to influence the price; the market is then also defined as imperfect, because if they enlarge their output they reduce the price against both others and themselves. By reverse argument, this condition is also called monopolistic

competition, because it seems to imply that these dominant producers can raise the price for others and themselves by reducing their own outputs; or even any one of them can do this to some extent. At present, nothing more is assumed than competition, or absence of agreement between the producers.

The idea of perfect competition ought to be related to its economic background. When producers were very small and numerous, business for each of them was local; it is the development of transport which causes business to fall back on a few centres, where the producers are larger and serve wider markets. Now, if 'pure' competitors had each sent his supply to a central depot for distribution, it is true that the price fixed at that centre would not change much if at all by the failure to deliver of any one of them, or by an increase of his small output. But central dealing is not the economic background of this phase of industry. There are local markets and, if any one producer increases or limits his supply, he is likely to alter the price for himself and his neighbours. If A's price is reduced, that of B will follow, so that what may be called the 'A to Z' rule will affect the whole market.

On the other hand, when there are some producers large enough for their output to affect price, the economic background is different. The market is organized by trade journals, and the market for each producer is wider in extent; he may sell only a small part of his output near his manufacturing plant. What is most important is that the intensity of his competition with other large-scale producers cannot be assumed to have declined. On the contrary, the history of Trusts and Combines shows that it was the intensity of the competition between large producers which led to them. The

problem of 'monopolistic competition' is therefore not a simple one. The general line of thought may be followed that, if there are large or dominant producers, it is on the whole probable that the standard price of the market will be higher than if no one was in such a position. But it is a question of the facts of business psychology whether this result, or something nearer its opposite, will really happen. We cannot, without particular argument, put more into the definition of competition than that it is the rivalry of alternative supply. There are some further technical conditions to keep in mind. For, if it is the case that there is any range of constant costs when a large producer is producing to capacity, no one is in a position to force a rise in price by limiting his own output, since his competitors can supply the difference without increasing their costs. It has been argued that such constant costs do obtain, so that there is a range of alternative supply at standard price.

We find then that the standard price which will maintain the whole supply is related to an average, a margin, and a minimum; the idea of what is representative or typical comes in under the concept of efficiency. The standard price is the minimum average cost of the marginal volume of supply of efficient production. We have seen what 'efficient' means. Marshall made the word equivalent to his term 'representative'; it means, in his definition, 'a fairly long life, and fair success, normal ability of management, and normal access (this is an important word) to the economies, internal and external, which belong to that aggregate volume of production'. He assumes competitive relations in the broad sense of the term which is here adopted. He does often say, and was fond of emphasizing it to his pupils, that efficient (or representative) business has

always some element of monopoly; that is the 'custom' or trade connection of the business. But this by itself is not a power to raise prices; it is nothing but the fact that the demand of the market can be split up in various ways, one of which is to add the parts of the demand supplied by each producer. There must be 'custom'; it is an aspect of efficiency as here defined; whether custom can be exploited because it is custom is a different question.

We may consider the idea of standard price and cost by supposing a producer about to enter the market. The market has a price, which he has to meet when he is fully efficient. He must sell at that price before he has a regular custom, and while he is still a high-cost producer; but he projects a scale of production at which he can come down to the ruling price. He does not argue that his own output will depress that price; because there are producers leaving the market, and others losing their 'efficiency'. Taking the ruling price, he has to consider how much to invest and how much to produce. The ruling prices of labour, material, and auxiliaries of supply, are also given to him. These are the variable costs, to be added to the fixed costs of his investment. The fixed costs are rents, and interest on all his capital, borrowed or subscribed; he must reckon on meeting these when he is established. The two conditions, that there is a given price to meet, and that average total costs must then be at their minimum, are sufficient to decide the amount of investment and the rate of output.

But as a rule, he does not reach this position at once. He has to obtain a custom and a place in the market. His investment is made in stages, and it is for this reason that the marginal element enters into the case. As a business grows, it either adds new departments or sets

up or obtains new plant, and these are liable, not being his first choice, to be less efficient than the original investment. He has to build higher on the same location, or find another location. These extensions of his investment must pay for themselves, and cover their full average costs. The marginal output of a business is likely to be more costly than the rest, and it is a volume of output, which can be specified. Established businesses are usually in this condition of having a volume of output that is marginal, and high-cost. The entry of new businesses is favoured by this fact, but they will have themselves to make similar marginal extensions. Thus the standard price becomes the minimum average cost of the marginal volume of supply of efficient business. It remains true that there are businesses whose minimum average costs are above this at any time, and others whose marginal costs are below it; and that a particular business has part of its costs more than covered by the price required for its marginal volume of output. Hence the great variation of profit and loss among the businesses which at any time are maintaining the output at standard price.

It is to be noted that these 'intra-marginal' gains are a chief source of the reserves of business, and of the expense of further development. They do not all pass into personal incomes, of individual or joint-stock investors. To an increasing degree, they go back into the industry. This fact lessens the significance of the difference between the marginal volume of output and the rest of it, and tends to make the general average approach the standard cost, if a cost of development is included. And, for new members of a joint-stock enterprise, intra-marginal profits are discounted in the price of shares. Of course, also, intra-marginal costs

are to some extent equalized with marginal by rents.

The idea that the standard price, at which a group of changing producers will maintain a rate of supply, should be regarded as the cost of a 'representative' producer, is not simply one of economic theory. The Balfour Committee, in stressing the great variety of costs of different producers, took as its standard for some industries 'the average of a large number of undertakings considered to be representative of the whole industry', or the 'typical scale' of production. Producers who are at any time less than 'efficient' for any reason cannot pass their high costs on to the price, but must take the price which depends on 'efficient' production. 'The price cannot be less than the cost of production plus a profit. But what cost of production? Producers differ in ability and opportunity. The competition of the efficient producer makes the trend of price toward the more efficient cost plus a profit. The less efficient makes a smaller profit, no profit, or a loss. The highest cost of production does not fix price.'¹ Later than this, it is reported that, for determining war-time prices for cotton, 'the proposal is that margins should be based on the cost of production in representative efficient mills running full time'. In evidence to the Sankey Commission on the Coal Industry, it was similarly argued that the cost of the 'worst' mines did not fix price, because of the influence of the more efficient, but that the same mines were not always the worst, because of changing conditions.² Committees formed under the Safeguarding of Industries Act had to consider the fair price to protect, and we find them using in one case the average cost of

¹ *Industrial Efficiency*, vol. 2, pp. 8, 177.

² *Sankey Commission, Evidence*, Q. 661-9, 6981 seq., 7076-80.

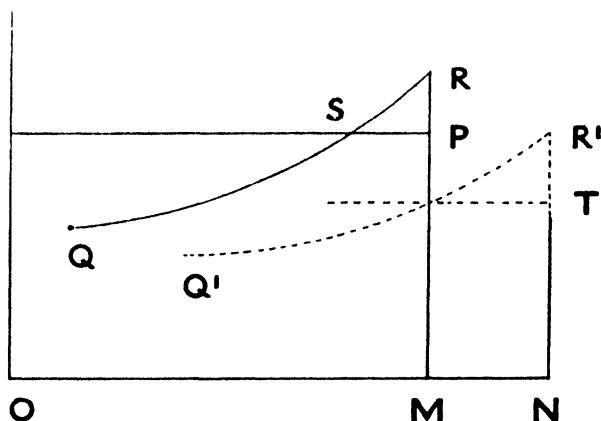
certain firms taken as 'representative of cost of production in the industry', and in another case of two of the chief firms chosen as 'representative of the industry as a whole'. In the United States, there were price-fixing bodies which had to decide the war-time price which the government should pay for, e.g., copper, and they took a price which covered nine-tenths of the output as the 'Plimsoll Line' which kept the whole industry safely afloat.¹ Marshall speaks of the 'representative firm' or firms as definite producers such that, when you know their average full marginal costs, you know what the market price for all must fluctuate about, in order to maintain the rate of total supply.

The 'efficiency', of which representative business is taken as the norm, has several aspects besides the age and size of such businesses. The full use of economies, internal and external, relates sometimes to particular aspects of the structure. Thus, in iron and steel, the representative business is an 'integration'; it owns its own coal mines and blast furnaces, as well as its finishing steel works. In other industries, like cotton, this is not typical. Or again, it may or may not be typical to distribute the plant, instead of having a single location. As a rule, representative business is large-scale, as scale goes in each industry, provided it maintains a proper elasticity of adjustment to new techniques.² In many cases, too, it has more than one final product, so that the standard cost for any one of these requires an estimate of its liability for the total overhead costs.

The diagram shows how the argument can be presented. There is a supply of O M units and the price is

¹ Prof. Taussig: 'Price-fixing', *Quarterly Journal of Economics*, vol. 33.

² Balfour Committee: *Metal Industries*, pp. 33, 89.



$M P$. The line $Q R$ shows the full costs at which different businesses, placed from left to right in the order of their efficiencies, are able to produce. Those between S and R are, at the moment, high-cost producers, who are not covering their full costs at the standard price $M P$. Some of them will leave the market, others will work their way to a better position in the line $Q R$. Others, now between Q and S , will, for different causes of lowered efficiency, find themselves between S and R . All the time, the price-determining cost will be $M P$, and representative conditions will be around S . $S P$ was found in Taussig's inquiry to be about one-tenth of the supply. Other figures were given by the Balfour Committee for groups of industries to show the nature of the line $Q R$.¹ This is the line called by Marshall the 'particular expenses curve', on which R will coincide with P only under certain assumptions which do not generally obtain.² This line is not the supply curve. That is the locus of the price-determining cost $M P$

¹ *Ibid.*: *Industrial Efficiency I*, p. 464.

² *Principles*, App. H., p. 811.

as the output changes from M to another quantity, N . It will carry with it a new curve of the same form as $Q R$. The particular expenses curve is the flashlight view of the industry when it is regularly producing a supply which fluctuates about the amount $O M$, at a price which fluctuates about $P M$.

It is a well ascertained fact that, as the volume of the market increases, the typical producer works on a larger scale. This is, in fact, one of the ways in which the economies are made which enable the standard cost to fall, or which control its rise. The cost-curve of a typical producer is U-shaped, and this can be shown to be the necessary result of a given investment with variable running costs. When the scale of production changes, we move from one such curve to another. Any U-curve is not a supply curve, nor a short-period, nor a long-period curve. It is a phase-curve. A movement from one point to another on such a curve shows nothing but the average cost of running more or less full; this is *not* what is meant in economics by the law of decreasing or increasing cost. In the fact that running full is cheaper than running short, there is nothing to explain. This is false decreasing cost. True decreasing cost is a relation, not between points on the same phase-curve, but between similar points on different phase-curves, whether these are the minimum or any other points. If therefore we join such similar points on the phase-curves of representative producers, we get the movement of standard price, but the slope of this movement depends on the change of the whole output, not on that of only the particular producer whose phase-curve we have drawn. In general terms, this is the nature of the market supply curve in its relation to the costs of representative production; it is called the long or long-period

supply curve. In the diagram, *P* and *T* are points on that curve. It is on its form that depends the question whether scarcity is being organized away, and a better standard of living made possible, for an increasing population or demand.

It has been said above that we have to be careful about arguing to diagrams or from diagrams and the definition of the supply curve just given at once raises such a problem. For if we join similar points on a number of phase-curves, all of which are U-shaped, any regular line will cut some or other of these curves; this is plain if we join the minimum points, so that the problem would exist even under what is called perfect competition. The supply curve of complete adjustment to a certain output would be above the phase-curve for running short, so that it would be better to invest for an output of 10,000 and run short, than to invest for running at capacity for an output of 9,000. If we try to make the long supply curve fall below all the phase-curves at every point, as some authors postulate it must, we have to draw it as an 'envelope' of the successive phase-curves, that is, as a tangent to them all. But we cannot do even that without requiring producers to behave in a certain way in order that we may draw a tangent. We cannot avoid this difficulty without giving up the assumption that there is a typical scale of output for *every* change in the market. Changes in scale are not so continuous as that. It is reasonable to suppose that, for any phase, there is a range of constant minimum costs, by the use of reserve capacity; and that a point on the supply curve is taken at the centre of the range, for each phase. The supply curve would then be resolved into a certain number of points of standard costs, depending on the stages of change of typical scale. For different industries,

the points we could mark would be differently spaced. This degree of vagueness appears to be unavoidable.

The movement from one phase, in which the representative producer is on a certain scale of output, to another phase, in which that scale is larger, so that the standard price changes, reflects the human problem of maintaining or improving the standard of living. It takes us back to the problem set by Malthus. The diagrams only illustrate it in skeleton form. How it can be done, without changes in invention or in discovery of new sources of supply, depends on the argument already presented on the nature of the internal and external economies of organization.

It was assumed by Marshall that the movement from one typical phase to another is the result of the strain put upon the earlier phase by fluctuations in the demand. Some article is more wanted than before, for its own sake, or because something has happened to its near substitutes, or because of a new market for it. These are 'short-period' changes, in which the producer has not yet changed the scale of his investment, or his fixed charges, but has to work at higher costs for labour (or extra labour-time) and for material. He does not alter the scale of his investment unless such a change in demand appears to be a settled one. Then he adjusts his investment to the new demand, and is on a new phase-curve. The fluctuation may recede or it may not. Apart from this uncertainty, the adjustment to a new phase takes time. While Marshall agrees that such fluctuation is the intermediate stage between one phase and another, it seems also to be possible that a typical producer might himself foresee economies of a larger scale, so as to make and not to wait for changes in demand. The importance of the 'short-period' line or curve is that, whatever the

phase, the producer is usually working on it, above or below the standard cost which still represents the phase or scale of investment.

Obviously, since the scale of investment has not been re-adjusted, the short-period curve is only a question of variable costs, of labour, auxiliaries, and materials. It is here that a different use of the word 'marginal' comes in. For even the marginal plant of business, in the sense used above, can be worked under greater or less strain according to fluctuation of demand. If demand changes upward, the producer will ask and get a price which covers the extra cost of expansion, in depreciation, or over-time wages, or more expensive materials; if it changes downward, he can only get the price it allows, as long as it covers his variable costs for reduced supply. In an upward change of demand, these marginal costs will go above the average costs shown, for the same expansion of supply, on his phase-curve. Why, then, is he not content to go on his average cost-curve itself, the cost-curve of the existing phase? Partly because that did not allow for changes in the unit cost of his labour and other expenses, but only for changes in his output at their usual costs: but chiefly because, if the demand changes downward, he *cannot* remain on his average cost-curve, but must sell below it, as long as he gets prime costs. If he did not get the short-time profits on an upward change of demand, he could not compensate for the short-time losses on a downward change of demand. These short profits and losses are called 'quasi-rents' by Marshall, because the equipment is in a phase of temporary fixation, as land is always. It can be shown that this short, or 'marginal' cost-curve (in this new sense) cuts the average cost-curve at its lowest point, that is, at the standard price and cost which

represents the phase. In a flashlight view, the producer is somewhere on this short or marginal cost-curve. But all the time, the standard price and cost are those of the marginal volume of supply in the other sense of the word. It is the movement of this latter marginal cost which is of importance to progress.

We have now to return to the general assumption of competition. If there are strong producers in the market, so that a change in their output can affect the price, is it a good general presumption that the cost of marginal production, about which fluctuation takes place, will be above the minimum average cost? This is socially of great importance. It is out of the enterprise of such strong producers that we expect progress to come, and it is an antinomy if the result is to hold standard prices above minimum costs. But this is actually the result of the recent analysis of what is called 'monopolistic' competition. In the work of Cournot, competitive conditions were derived from those of monopoly, by first supposing a complete monopoly, and then multiplying the monopolists; so that an element of monopolism continued, as long as the producers were not indefinitely numerous. The modern analysis therefore revives the idea of absorbing the problem of competition into that of monopoly, and the question is one of the psychology of rival producers, that is, of what sort of diagram we can argue to.

This is independent of the question whether the producer who is an 'imperfect' competitor has a part of his custom which is not only habitual but also preferential. Preferential custom exists, e.g., between con-denominationalists, or to encourage small producers, or for other reasons: it implies that a part of the custom has a small

elasticity of demand in respect of that producer. It may be possible to exploit this up to a point, though that is not the best way to hold a preference.¹

The general argument is, that a strong producer, whose investment is adjusted to a demand of, say, 10,000 units, will, without any arrangement with others, put his price up to monopoly point and see what happens. The demand will then shift to other producers, or to new producers. This will cause the demand curve of the producer considered to fall, until it becomes tangent to his phase-curve, at a point below his full capacity. There will therefore be an equilibrium of running short, at a price higher than minimum average cost. But the producer who thus attempted a price higher than cost will have done himself no good, since he will be back to his average cost-curve, but at a restricted output. The equilibrium will be kept, because one point on his average cost-curve is as good to him as any other, and running short is less trouble or, perhaps, creates reserve capacity. The community is, however, deprived of the full advantage of large-scale production, and of full employment. The argument has therefore an important reference to the development of private capitalism.

On the other hand, it is commonly held by reference to history, that large-scale capitalist industry leads to forms of competition which are so intense as to be described as anarchic, cut-throat, and ruinous, and that monopolism by the method of combination is a reaction against prices which are in danger of ruling intermittently below minimum average cost. Hence the meaning of the question whether we are arguing to diagrams or from them. We have to allow for what cannot go on diagrams, the psychology of producers

¹ v. Marshall: *Industry and Trade*, p. 182.

who are strong but quite independent, and subject to rivalry of supply; but the argument from the diagram still requires attention, and it has seriously influenced the net expectation of the economy of large-scale organization.¹

The calculation of an investor has been outlined above, and that assumed that he expected the demand curve of his custom to cut his cost-curve at its lowest point. But to this it is objected that in that case there is a part of his output for which the extra costs are above the extra income obtained by producing that part. It has of course to be remembered that his whole output is effective in reducing his fixed unit costs, and that the whole unit cost may be a more natural thing to consider than the equation of marginal cost and revenue. And, if there is a part of his full capacity output which can be debited with a net surplus of cost, it may still be one of the cheapest forms of advertisement to run at minimum cost and incur that charge, since average costs are also recovered.

A second question is whether a strong producer who has rivals will take the risk of fixing a monopolistic price without any understanding with his rivals. If they have any range of constant costs around their capacity output, he risks a dangerous shift of custom. But if, as must rather be supposed, his rivals act just as he acts, and also aim each for himself at a monopolistic price, where does the demand shift to? New producers are high-cost producers. On this second alternative, the result seems to be an indeterminate condition of prices. We cannot take the diagram of one rival without considering the similar action of the others, and,

¹J. Robinson: *Economics of Imperfect Competition*. E. Chamberlin: *Monopolistic Competition*.

without agreement, similar does not mean co-ordinated.

The third question is whether an equilibrium of running short could be maintained. The producer is back on his average cost-curve for a lower output, and has done himself no good; he is insecure against a rival who incurs the disguised advertisement charge, if not also the sensible policy, of running full. Again, it would seem natural for a producer whose attempt at independent monopoly has got him into a condition of running, at say, 90 per cent of his capacity, to readjust himself to this position, instead of holding surplus capacity. This means that his phase-curve would have a new minimum at his shortened supply. But then the whole process of the diagrammatic argument would start all over again.

The purpose of this section has been not merely theoretical, and we have to keep in mind the social bearing of the question. The efforts of labour are meant to overcome scarcity, by organizing the available factors at the base of the economic structure. To overcome scarcity, we rely on the power of organization, since we cannot rely indefinitely on discovery or invention. The index of the reduction of scarcity is the falling cost of supply. That is the supply curve, or schedule. Large-scale production is one of the chief causes of the economies which can relieve scarcity. But if running short of capacity is an incident of the 'monopolistic' competition of large producers, one of the chief forces of economy is impeded by its own development; the supply schedule becomes the locus of something above minimum cost, and employment is restricted. Monopoly is thought to be a danger of high capitalism because of such restrictions and scarcifying tendencies, to the extent that its dangers have been made one of the grounds of nationalization. This objection to a result of high capitalism

would be stronger if, even short of monopoly by combination or agreement, the tendency was for producers to find an equilibrium of short supply. Such a conclusion has to be considered in relation to the sense of the words which have been found to apply to large-scale competition in its historical aspects, and to the consideration of the psychology of rival supply between strong producers.

CHAPTER 3

THE LAISSEZ-FAIRE DOCTRINE

The early history of the maxim, and the place of D'Argenson in economic thought. Its treatment by British economists was not dogmatic. It is necessary to discard the phrase, and to define separately the different ideas which it now conceals. Its final application to the action of government itself shows that it has ceased to be a significant phrase or principle.

THE British economic system from 1800 to the First World War is associated with a system of thought which is called laissez-faire. This phrase shows that the idea came from France. But these are ordinary French words, which could not have become a maxim unless in some special way they had come to be isolated and underlined. Unless they had been so isolated by French writers, they would not, in an English translation, have been left in italics in their original language. It was not English writers who foisted the phrase on French writers by giving it the prominence in English books of an untranslated pair of words. It had been separated from its ordinary use in cursive writing by French writers themselves, so as to be made a maxim.

The English classical economists did not use this phrase at all, until Mill pronounced it a rule of general practice in 1848. It does not occur in Adam Smith, nor Malthus, nor Ricardo, nor McCulloch, nor Senior. When Bentham wished to express the idea of non-interference by government, his phrases were English ones—'Let us alone', or 'Be quiet', or 'Stand out of our sunshine'. He used these phrases before 1800,

when he was half a century nearer than Mill to the French School of Economists. He was not averse to foreign phrases, for he speaks of public *Agenda* and *Non-Agenda* in relation to what he calls *Sponte Acta*. There is a tendency to enhance phrases or maxims, especially in the sphere of law, by expressing them in foreign words; we do not say 'firm ground' when we mean *terra firma*. If Bentham and the English economists before Mill had known of laissez-faire as a maxim of policy, they would have said it. Yet Adam Smith was the friend of Turgot, and was a student of the writings of the French School which preceded him; where then did laissez-faire come from, and why was it a lost phrase until Mill broadcast it, so that it came to be almost the definition of English economic thought?

Maxims are ordinary words which on some occasions are used with special emphasis in some reference. No doubt many people before Queen Victoria were 'not amused'. The 'impatience of taxation' is a phrase usually ascribed to Gladstone who emphasized it, but he got it from Northcote, who got it from its use by Castlereagh on an important occasion in 1816; but Bentham had used it as an ordinary remark before 1800. 'Finance is the sinews of war' said Sir F. Burdett in a Commons debate in 1798, when it passed without notice; on some later occasion it was recalled and made current. Mill made the 'wages fund' an economic maxim fifty years after the 'sacred wages fund' was defended in Parliament against the triple assessment of Pitt. The 'invisible hand' is ascribed to Adam Smith, though D'Argenson had much earlier written that 'le gouvernement invisible de Dieu laisse agir les causes secondes'. Who would now know that 'an Englishman's house is his castle' was first said in a Commons debate on the

cider duties, in the eighteenth century? The occasion which gives currency to a maxim is either a notable event, or its use by a person of high authority.

The history of *laissez-faire* began with its use in a particular sense on an occasion of which there is no contemporary record, but which was recalled some seventy years later as being well known. In being so recalled, the maxim was used to support a wider idea. And the ideas which such a phrase can be used to support are plainly so various, both economic and political, that it easily came to absorb extensions of its use, until it reached the condition of 'all depending what you mean' by it, which is its present condition. There is no doubt to what question it was first made an answer; but now it is necessary to know distinctly the question—whether it is free trade, or private enterprise, or the *status quo*, or competition, or capitalism—before the maxim has any relevance.

In the Free Trade debate of 1846, which occupies about 1,500 double-column pages of Hansard, the phrase *laissez-faire* never occurs, and no important speaker referred to this expression of a principle. But one private member referred to the 'short answer which had been given by the French merchants, when asked by Colbert what best could be done to advance their trade and serve their commerce'. Their answer was, 'Pray, let us alone.' Let us follow this clue.

In 1751, there was published in France the *Journal Oeconomique*, probably the first economic journal, in monthly numbers. In the March number, an article reviewed a book published in 1750 by an Italian mercantilist, the Marquis Belloni. This brought an answer in the form of a letter to the Editors in April,¹ in which

¹ Translated in *Select Essays on Commerce*, etc., London, 1754.

an anonymous writer questioned whether there was not much to be said for more liberty of trade. And he said that 'it is reported of Colbert that, when he convened several deputies of commerce at his house, and asked what he could do for the benefit of trade, the most sensible and plainest spoken among them replied in one word, "*Laissez nous faire*". Have we ever sufficiently reflected on the good sense of that short answer?' This is the first reference in literature to the origin of the maxim. The writer proceeds to argue for freedom of trade, and protests against those who pretend to an 'integral and universal capacity' of directing all commerce, a task that is beyond them, since '*non datur scientia*'. It is known who wrote this letter. It is definitely ascribed, in the French *Biographie Universelle* to the Marquis D'Argenson, of whom more later; and similarity of phrases in his later published works verifies this conclusion.

Who was this 'most sensible and plain-spoken' merchant, who could be remembered seventy years later for his retort? We are told by the Physiocrat Turgot, the friend of Adam Smith. There was a merchant, later an official, Jean Vincent, Seigneur de Gournay, who was not an author, but was personally intimate with the Physiocrats, and was so zealous an advocate of their views on freedom that the extended phrase *laissez-faire et laissez-passer* is attributed to his conversation in private and at meetings. When he died in 1759, Turgot wrote his eulogy, especially for his defence of economic liberty, and said in that connection that '*on sait le mot de le Gendre a M. Colbert; laissez-nous faire*'. Turgot speaks as if the occasion, and le Gendre himself, were well known, although no contemporary record of the meeting has ever been found. Colbert had many meetings with

merchants, and it has been guessed that this one took place at Lyons about 1680. A person called le Gendre was the author of a mercantile handbook published in 1657.¹ This at any rate is how *laissez-faire* became a phrase some 300 years ago, but a phrase of the marketplace, which had to wait a while to be endorsed and propagated in economic writing. Did Adam Smith never hear about this from Turgot, or did the phrase not catch his ear? The Physiocrats themselves neglected it; Quesnai never uses it, preferring, in his own list of maxims of economic government, to use a longer phrase, *l'entière liberté du commerce*, when the shorter one might have been expected.

The reason is that both le Gendre's retort, and even Gournay's extension of it, were entirely topical, and meant something far narrower than the economists, French and English, came later to propose and defend. No one who objected to what was afterwards called *laissez-faire* could have objected to what *laissez-faire* first meant. Colbert was an able but dictatorial organizer of French industry and trade, on which, in the interests of the revenue and of effective competition with foreign goods, he imposed a strict system of guild regulations. There was no freedom of occupation or of daily business; bankrupts could be penalized, and inefficient producers pilloried; his inspectors were hated. His system still obtained in Gournay's time, and Gournay, says Turgot, 'was astonished to see that a citizen could neither make nor sell anything without having bought the right to do so at great expense in a corporation, and that, having bought it, it was still sometimes necessary to go to law to determine whether he had really acquired the right

¹ Oncken: *Die Maxiime lassez-faire et laissez-passer* (Bern, 1886), of which an English translation is much to be desired.

to make or sell precisely this or that article. He could not see it to be useful to society that a manufactured piece of stuff should involve legal procedures and tedious discussions in order to ascertain whether it conformed to a complicated system of regulations, often difficult to understand, nor that such discussions ought to be held between a poor manufacturer who could not read and an inspector who could not manufacture, nor that inspectors should regulate the length and breadth of each piece of stuff, and the number of threads it was to contain, nor that industries should be regulated by apprenticeships of ten years for trades which could be learned almost in ten days, etc.' To make what you like in the way you like is Adam Smith's freedom to invest your labour as you please; but the phrase which began in 'freedom to make', and still literally means that, has somehow come to apply to other ideas which are no sort of translation of it. The purely topical nature of le Gendre's retort is also shown in its third word; 'let us, not you, do the business'. Before it came into economic literature it had to shed this third word, so as to become a principle of policy instead of a slogan of merchants.

Colbert's regulations were not so absurd as the quotation from Turgot's eulogy of Gournay would make them appear. He wished especially that French fabrics should compete with English ones, for which purpose they had to be strictly according to the English sample, down to the last thread. The trade mark, thus maintained, gave the monopoly to the corporations who could use it. And it has been argued that this restrictive policy was sound in the seventeenth century, to protect a nascent stage of French commerce. But it outlived its usefulness, so that by Gournay's and Turgot's time it

had become burdensome and needlessly monopolistic.

We do not know that Colbert's merchants were free traders, as we use that phrase, and probably they were not; for even Boisguillebert, a precursor of the Physiocrats, and nearer to Colbert's time, was not in favour of free import. *Laissez-faire* began by meaning what the words say, freedom of occupation. By the time it appears in literature, it has been generalized, so as to include freedom of commerce. This has been done by dropping the third word *nous*, so as to detach it from the particular occasion. The addition by Gournay of *laissez-passer* also shows that this was not included in the original meaning. Of course, free trade is not any translation at all of *laissez-faire*. The confusion between freedom of business and freedom of commerce began early. If there is free trade, producers have a system of prices and conditions to reckon with in their business; if there is Protection they have a different system. Their business freedom is quite a different thing from a national policy, and the tendency of producers in many countries is to favour Protection as an actual stimulus to their enterprise. But somehow, between Colbert's time and the first literary enunciation of *laissez-faire*, it had begun to absorb its wider meaning. It drops the third word, and the first one masters the second.

The author of *laissez-faire* as an economic principle is the Marquis d'Argenson (1694-1757), whose life fills the gap between the Colbert regime and the first writings of the Physiocrats. A number of first things are associated with his name. He wrote, as we have seen, for the first Economic Journal, and was a member of the first Economic Club, the Club d'Entresol. He joined this Club in 1726, so that it was prior to that

founded in Glasgow in the 1740s, of which Smith was a member, and which was claimed to be 'the first political economy club in the world'.¹ The Entresol was dissolved in 1731, when its interest in and influence on current affairs were considered dangerous. He is the first to relate the meeting with Colbert and the retort of le Gendre, but without his name; and he is the first to utter *laissez-faire* as a principle of public policy. His reputation is that of an upright and able critic of the court of Louis XV, and of his ministers; for about two years he was the Foreign Minister of whom it was said that the affairs with which he was charged were really foreign to him. In public life he was *maladroit*, and his unpopularity with the regime earned him the nickname of *La Bête*. He wrote voluminously, but his timidity kept him from publishing; his manuscripts were circulated to friends (which was the custom of the Club), and were finally deposited in the library of the Louvre. There was no complete French edition of his work until the middle of last century, and only his letter to the Journal, already referred to, has been translated into English. He was therefore unknown to the early English economists, and this may be the reason why his abrupt statement of *laissez-faire* was not taken up as a phrase by them. Even now, French and English dictionaries and encyclopaedias know only enough about him to misquote his political maxims. It was Gournay that Turgot eulogized for his private advocacy of *laissez-faire*, *laissez-passer*; but Gournay wrote nothing, and does not belong in the literature of the subject.

To D'Argenson, *laissez-faire* was both a political and an economic principle. Better government, he said,

¹ Rae: *Life of Adam Smith*, p. 91. D'Argenson's *Mémoires*, vol. I, p. 91 *seq.*

means less government. This is to be understood against the conditions in France at his time, with its high bureaucracy and officialdom. In economics he meant both non-interference with industry and free international trade. On this latter question, he is more outright than Adam Smith, who is rather at the end than at the beginning of the argument conducted in France by D'Argenson and the Physiocrats.

D'Argenson is the undoubted literary author of *laissez-faire* in two words, whereby it detached itself from its use on a particular occasion; it became let alone, not merely let us alone. There is no doubt what he did with the maxim; he framed it. It had occurred before in the cursive script of writers like Boisguillebert; but, to a French writer, the phrase did not separate itself, as it does when an English translation leaves the phrase italicized in French, and so gives it an unmeant prominence. Boisguillebert (1646-1714) can be regarded as a precursor of the Physiocrats, one who anticipated their ideas of the 'natural order', and who said that, for example, '*il n'y avait qu'à laissez-faire la nature, comme partout ailleurs*'. Probably many French writers used these two words in this cursive manner. D'Argenson is not an expositor of a 'natural order'; *laissez-faire* is to him a matter of personal action and public attitude. He took the phrase by itself, starred it, and framed it, but in secret writings. His eulogy was written in the letters of Voltaire, his friend and fellow-student. Here are the first statements of the maxim:

'Il est vrai que c'est la seule et entière liberté qui peut bien régir le commerce, l'agriculture et les mœurs. C'est sur quoi je travaille moi-même depuis dix-huit ans, ayant remarqué que 'pour mieux gouverner il faudrait gouverner moins'. Je blâme ici les louanges qu'on donne

à notre conseil de commerce, et le proposition d'établir une commission pour l'agriculture. Ce sont-la des restes du vieil homme et des idées de tyrannie gênante.

'Eh, morbleu, laissez faire.'

'Le commerce est tombé en desuetude et en ruine par la stipulation de gens trop riches, qui ont indiqué des lois et par conséquent des genes, des vices, et des contraintes. Ah! qu'il en servit autrement si on laissait faire la fourmilière. On travaille trop, on gêne trop; on devrait se reposer davantage, et tout irait mieux.'

'Laissez faire, telle devrait être la devise de toute puissance publique, depuis que le monde est civilisée. Les hommes sont sortis de la barbarie; ils cultivent très bien les arts; ils ont des lois, des modèles, des essais en tout genre pour connaître ou sont les bonnes pratiques. Laissez-les faire, et vous observerez que là ou l'on suit le mieux cette maxime tout s'en ressent. Tout ce que échappe à l'autorité et laisse l'action de l'homme plus libre prend son essor et fructifie.'

'Notre richesse consiste en une bonne et universelle agriculture, aux manufactures par les habitants qui ne peuvent vaquer à l'agriculture; à la circulation intérieure, non de l'argent et des bien fonds, mais de toutes marchandises mobilières, à faciliter cette circulation réelle. Après cela, laissez faire, laissez les étrangers venir prendre nos marchandises. Détestable principe que celui de ne vouloir notre grandeur que par l'abaissement de nos voisins.

'Laissez faire, morbleu, laissez faire.'

In these statements from his *Pensées*, not published till 1857, laissez-faire is made, as he calls it, a maxim; and the earliest of them is dated 1755. The maxim is by itself a claim for personal freedom in industry—'*qu'on laisse faire chacun en droit soi, au lieu de gêne et de precautions mal inventées*'—as he elsewhere writes. He did not make a maxim of laissez-passer; that came later from

Gournay. But though, like Adam Smith, he believed the home trade to be more valuable than the foreign trade, and though, like the Physiocrats, he had a bias in favour of agriculture, he was a thorough free trader, and held that 'commerce should be as free as air', without any of Smith's well-known exceptions. This combination of free enterprise and free trade is not a necessary one but, when the same person or, as happened later, the same party holds to both, the same phrase becomes the cover for a broad attitude of thought; and, if the attitude of thought is still further extended, the phrase becomes a label for persons or parties, or for policies into which it cannot be translated.

Colbert had been an able, broad-minded, and well-intentioned planner of the French economy. The reaction against his system had been led by precursors of D'Argenson, especially by Vauban and Boisguillebert; D'Argenson inscribed the motto of this movement. He is called by Cossa '*le Paladin français de la liberté économique*', but to most historians only his name is known. Had he published in his lifetime, he would have taken a place in the economic literature of an argument in which Adam Smith was a late comer, and his maxim would not have had to wait for Mill to take it up.¹

He speaks, in the above quotations, both of his maxim, and of its use as a plan (*devise*). It came to be supposed later that *laissez-faire* was the opposite of any plan or policy. There is neither, when a course of events is not brought under consideration at all. It has always been a difficulty that, since policy and plan are words of positive meaning, non-interference seems to imply absence of purpose. But, as will be argued later, it is

¹ A. Alem: *D'Argenson Economiste*, Paris, 1899, gives him a place.

purposive when it is the result of consideration of the alternative in any case.

D'Argenson becomes the literary author of the maxim of laissez-faire only by our posthumous knowledge of what he wrote. Gournay might have been the author, if his private notes and memoirs had also come to be published. In 1752, he translated into French the works of Child and Culpeper, and wrote notes on them which, Turgot says, came in volume to as much as the text, and were circulated to friends. 'There is scarcely any important question of commerce or of political economy on which he has not written several memoirs or reasoned letters' and circulated them without having kept any copies. But when his translation was published in 1754, the publication of most of these notes was forbidden by the censor; Turgot has remarks on a few of them. He died in 1759, only two years after D'Argenson, and it was Gournay whom the Physiocrats regarded as the hero of the liberal economy, for he mixed with them in his advocacy of 'laissez-faire, laissez-passer', while D'Argenson held aloof in his retirement. But we have D'Argenson's writings, and so he obtains the priority in economic literature. We know most about Gournay from Turgot's account of him, and in that account he incidentally recalls the maxim of laissez-faire, but refers it to Le Gendre, and does not suggest that its special use by Gournay was noteworthy. In fact, D'Argenson and Gournay expressed themselves in a phrase which was not taken up by the Physiocrats as a short title for certain of their economic opinions, and so it lapsed into the half-world of popular usage, until Mill picked it up in the condition in which he found it at his time.

The Physiocrats got to the same result by their appeal

to 'nature' and the 'natural order'. Evidently, the tendency of this philosophy is against a system of human controls. For what is 'natural' can be taken in several ways. It sometimes implies, or even defines, what is original, as in Hobbes' 'State of Nature', and this in turn implies what is either most simple or most fundamental, as regards either human conditions or human 'rights'. But the natural also implies the ideal, in respect of what is either just or advantageous or admirable; or the expectable, if there is no interference, or the inevitable, which interference can only delay. 'Naturally or rather necessarily' is a frequent phrase of Adam Smith. By an amalgam of these different meanings, we get the kind of natural system or order which idealizes what is most simple and fundamental in economic relationships, and this idealism takes, in its final phrase, the aspect of the providential.¹ Laissez-faire was a leaf out of their book, but not enough to be the title of what they had to say. And there was a censorship which seems to have restrained them from slogans against the government.²

Of the thirty *General Maxims of Economic Government* which the father of the Physiocrats, Quesnai, published in 1758, the second emphasizes the 'General laws of the natural order', and the twenty-fifth, printed in large capitals, claims the 'complete freedom of trade'. Here was the place to have ended with a watchword like laissez-faire as D'Argenson did; but it is not used. The index to the voluminous writings of Turgot shows that, apart from the reference to le Gendre, it occurs only once, when he says that 'if men have a strong interest in some

¹ Ritchie: *Natural Rights*, ch. 2.

² Martin: *French Liberal Thought in the Eighteenth Century*, p. 95, *seq.*

benefit you wish to obtain for them, *laissez-les faire*; that is the great and unique principle'.

Coming to England, we find the maxim used only once by Bentham when in a private letter in 1808,¹ he refers to his *Defence of Usury* as a case of the principle of *laissez-nous faire*; and then we have to go to Mill, who made it the title of his long study of the optional functions of government, and attached the label to 'those who have been called the laissez-faire school', since they think that the functions of government should be limited to 'protection against force and fraud'. It was here and by Mill that the classicists were given the label, and we shall shortly consider its relation to their opinions. His own position is that laissez-faire should be 'the general practice'; that the 'burden of proof' is on the supporters of public interference, to the extent of requiring them to show 'a strong case', or 'a great good', and not merely a balance of expediency, for any of the 'optional functions' of government. His exceptions are so numerous and so argued, and his general statements so sweeping, as in fact to mean little more than that public policy should be considered policy. If French must be spoken, he meant *prenez garde*, as did his predecessors.

In the half-century after Mill wrote, the growth of socialist opinion caused the alternative between public and private operation of industry to become the strong case of the argument. Mill suggested a combination of both methods in the same industry. But the label of laissez-faire came to be attached, not to private enterprise as such, but to several aspects of the system of private enterprise. Thus competition, monopoly, wage-bargaining, landlordism, capitalism, the trade

¹ Works, Vol. x, p. 440.

cycle, the *status quo*, as well as free trade, all came within an extended use of the old phrase. Political and economic interpretations also crossed each other. It was more used by objectors, than by supporters of anything; a general licence for criticism. As an example of the confusion of speech, it may be noted that while Dicey described 'Benthamite laissez-faire' as a 'war-cry' after 1832, Trevelyan observes that the Poor Law of 1834 'was based not on laissez-faire but on its opposite; it was pure Benthamism', and that Dicey regarded the same Act as a case of laissez-faire for a somewhat strained reason. Trevelyan concludes generally that Benthamism was 'in many respects the exact opposite of laissez-faire' because of its political controls, but holds also that free trade and the ten-hours Act of 1846 and 1847 showed that 'laissez-faire never obtained on all sides at once'.¹ Such various interpretations of scholars show how the meaning of the maxim was being diluted, or extended into vagueness. In *Past and Present*, Carlyle denounced laissez-faire and the Corn Law in the same breath, and appealed *against* laissez-faire to the justice and divine inspiration of the laws of Nature, so making it difficult to understand what Smith's invisible hand had to do with the principle.

We are at present following only the history of the maxim. The last phase came in this century, before the Great War. Enterprise is a good word, and it had tended to be specially associated with the private economy, leaving to the public economy the more routine idea of administration. But should there not also be public enterprise? Then what should public authorities be enterprising about? There might be an

¹ Trevelyan: *Social History of England*, pp. 538, 543, 548. Dicey: *Law and Opinion*, pp. 148, 202.

argument about the degree of their interference with private enterprise, or about the alternative between public and private operation of industry. But there are functions which only government can carry on; some of Mill's exceptions to laissez-faire were really of that kind. Then the government ought to be enterprising in perceiving these duties and in exercising them; this is public enterprise. Very good; but why call it laissez-faire, except perhaps to rescue the phrase from its unpopularity? The statement that 'we are all Socialists now' seems to have been first made by Harcourt in 1888, in the decade which saw a strong movement toward social betterment by public methods, and in that sense Marshall pronounced in 1907 that 'every economist of the present generation is a Socialist'. And therefore, 'a new emphasis is given to the watchword *laissez-faire*:—Let everyone work with all his might; and most of all let the government arouse itself to do that work which is vital, and which none but government can do efficiently. . . . So I cry, *Laissez-faire*; let the State be up and doing.'¹ This idea was endorsed by Keynes in 1926, under the title of the 'end of laissez-faire'. 'The most important *Agenda* of the State relate not to those activities which private individuals are already fulfilling, but to those functions which fall outside the sphere of the individual, to those decisions which are made by *no one* if the State does not make them.'² Thus the end of laissez-faire is '*Laissez-faire l'Etat*'; the principle is transferred to a higher sphere. It is buried in dishonour and raised in glory. There could never be any question that the State should do what it alone can do, and it would not be worth while to invent a phrase to express this. If

¹ *Economic Chivalry*, in *Memorials*, p. 336.

² *Essays in Persuasion*, p. 317.

there had been no history of the maxim *laissez-faire*, it might serve, though it would be clumsy. But it has a history, the central aspect of which is how far the State should do what private persons can also do; or, as Mill put it, what are the optional functions of government? In view of that, this last stage in the history of the maxim is either paradox or platitude.

Commonsense perceives that there are some advantages in controls, and other advantages in freedom from controls, and the same phrase cannot cover the choice of the mixture which commends itself at different times, or to different persons. It is therefore not surprising that the end of *laissez-faire*, which Keynes perceived in 1926, should also have been perceived at different dates over a long time before that. Mill wrote to Carlyle in 1833 that 'in the meantime that principle, like other negative ones, has work to do yet, work mainly of a destroying kind, and I am glad to think it has strength enough to finish that, after which it must soon expire; peace be with its ashes when it does expire, for I doubt much if it will reach the resurrection'.¹ Fifteen years later, in his *Principles*, he wrote that the principle should be 'the general practice to be set aside only by 'strong' reasons. The economist Cairnes in 1870, and Goschen in 1883, wrote on its demise, but only as far as purgatory, since they were free traders, and believed parts of the principle to be excellent. In the new social programme of the early eighties, Chamberlain announced its 'death knell', but only in certain respects. The end of the influence of its 'deadhand' was proclaimed in the Import Duties debate in Parliament in 1932, by speakers who believed in Protection and private enterprise.

The question between public and private spheres of

¹ *Letters*, vol. 1, p. 46.

activity cannot now be suitably handled by a phrase which has been so much twisted from its original meaning, and to which other meanings have accrued, into which it is not easy to translate it. We should agree with Oncken '*qu'on laisse passer laissez-faire*', and that any aspect of policy should be expressed in English as free trade, competition, private enterprise, or whatever kind or degree of control is in question at any time.

So much for the mere history of a phrase. There are several aspects of social and economic thought which help to interpret it.

There is first the question of 'interests'. When these are brought into this discussion, it is usually, however broadly, implied that there are grounds for some kind of public interference.

It is obvious that, within the framework of the law, every person acts according to his interest in deciding what trade or profession he is to enter. It was unnecessary for Smith and other economists to protest that this kind of freedom, to 'apply one's labour and capital as he chooses', should not be interfered with. This interest of an individual includes himself, his family, and a number of relationships which make up his 'life'. He is right to assume that he should act on this interest, and that he knows most about it. He cannot know what else it is in the public interest he should do. The framework of law sets the conditions on which he can act, and these conditions are the public interest as seen at any time. He can act contrary to the spirit of the law either by undue assertion of his own interest, or by failure to assert it, so as to make his work less effective. Smith was sarcastic about those who affected to trade for the public good, and Steuart had expressed this

before him: 'Public spirit is as superfluous in the governed as it ought to be all powerful in the statesman; and were everyone to act for the public, and neglect himself, the statesman would be bewildered.'

But when an 'interest' is emphasized, the reference is to persons who are grouped in economic classes, such as workpeople, employers, landlords, producers, or consumers. Their interests are 'vested' in some economic condition, such as high or low prices, profits, or rents, which affects them all as a group or class. Smith argued that the interests of merchants and manufacturers were opposed to the public interest, and Ricardo that the interest of landlords was so opposed. This means either that the course of events can turn, for short or long periods, to the advantage of these classes, or that, being groups of persons who can organize themselves, they can cause such a turn of events. One solution to this problem lies in counter organization of interests, such as is obtained by co-operative societies and trade unions, but the unclassed 'public' depends finally on the use of the framework of law and taxation in preventing or controlling the conditions which serve the group 'interests'.

Dicey has argued that interest is governed by opinion. 'The citizens of a civilized country, such as England, are for the most part not recklessly selfish in the ordinary sense of that word; they wish, no doubt, to promote their own interest, but they certainly do not intend to sacrifice, to their own private advantage or emolument, either the happiness of their neighbours or the welfare of the State. A man's interest gives a bias to his judgement far oftener than it corrupts his heart.' He is relying on Hume's doctrine of opinion, that 'though men be much governed by interest, yet even interest itself, and all

human affairs, are entirely governed by *opinion*'. Thus protectionists or free traders, monopolists or individualists, agriculturists or industrialists, may be supposed to believe that the conditions which are in their interest are defensible from the point of view of public interest; and there is no one to defend an interest except those who are directly touched by it. Smith said there were 'many cases' in which this opinion might be right; but this implies many others in which it is not, and he gave more examples of the visible than of the 'invisible' control of interests. Positive legislation, and repealing legislation, show that there are both kinds of cases. But interests are not, by this reference to opinion, cleared of anything but motive. An *emphasis* on interests is generally a claim for public action of some kind.

The law has to be framed so as to be strong enough for 'marginal' cases. What is forbidden or required in, for instance, factory acts, does not necessarily reflect on the general motives of employers. The law assumes the worst motives of the worst persons. 'It is a fair political maxim,' said Hume, 'that every man must be supposed a knave; though it appears somewhat strange that a maxim should be true in politics which is false in fact.' Bigamy is against the law, but the existence of such legislation does not reflect the general morals of the nation. Interference by law has usually to appear greater than it is. It 'lets alone' a good deal more than it seems to do.

In every branch of economic and social legislation there has to be a law which is the first of its kind. The occasion for this law is one or other aspect of the course of events. There could not be legislation about factories, companies, trade unions, or public health, until people had combined into groups for working or living. It is

obvious, however, that such legislation will tend to be behind the course of events, and will be delayed until that course has influenced opinion. Opinion, says Dicey, creates law, but only after an interval. The same applies to changes in the law, when the course of events has shown that there are new conditions. This lag of legislation behind the course of events means that there is a time when some conditions have arisen which are not yet controlled. These are the times on which social criticism fastens, and there must always be opportunities for such criticism. The criticism is often stronger after a law is passed than before it, and the law thus reflects on what was previously done or not done without it. Much of the criticism of conditions since 1800 is often expressed as if those who passed the laws which changed them were in some way culpable, and even now history is sometimes written as if we of the present day could be accused of the conditions out of which we have been legislated. The first law of its kind might, with perfect foresight, have accompanied the economic development which required it; but often, as in the cases of public health, or the early factory acts, not only is it behind the course of events, but a condition of emergency has to arise to bring about the law, or a change in the law. The government cannot be always legislating about everything, so that things are 'let alone' till opinion or emergency occasions legislation. This means in turn that progress is not the measure of welfare. There would have been more welfare in the modern period if social legislation had anticipated the events on which it followed, so that the difference between the beginning and the end would, in terms of legal provision, have been less; if, for example, trade unions had been as free in 1824 as they are today. In

1824, also, a man could be hanged for offences which are now regarded as trivial. But there would have been less progress had there been more foresight. In this respect, moral sense is in conflict with historical sense, so that we have what may be called the antinomy of progress. It is that antinomy which brings into the writing of economic history the accents of indignation and censure, as if the progress itself were almost culpable.

While opinion creates law, law also, as Dicey has argued, creates opinion; and behind them both there is the course of events which he calls the 'occurrence of circumstances' or the 'opportuneness of the times'. The course of events is, generally speaking, a phrase for the way in which persons choose to act within the existing law, and "it includes their inventiveness of processes and methods and forms of organized action. Since these cannot all be foreseen, the law is late on development, but apart from this there is what is called the 'spirit of the law', and this can be 'abused' by the marginal cases of those who take advantage of unforeseen conditions. One mining act created inspectors, and one employer held that while the law compelled him to take the inspector down the mine, it did not require him to bring him up again; short of such abnormalities as this, the course of events is a constant pressure on legislation. But, since law also creates opinion, there are periods of 'vested opinion', as well as of vested interests. Vested opinion cannot be separate from some interest or interests; as Dicey says, if you know the legislation of a period, you know something about the prevailing interest. And vested opinion must also have some support in the course of events. But in different degrees it may be abstract or empirical, affected, that is to say, by either social teaching or social experience. Its effect

is to resist changes in the trend of legislation, which may become so late on the course of events that it is only changed by emergency or breakdown; so much so that war can be regarded as a necessary occasion for the revision of a trend which has been uncritical of its tendency. Next to emergency, by war or economic breakdown, vested opinion is broken by the outbreak of leading personalities, who 'fault' the trend of what has been thought good enough. Vested opinion and the course of events are the evolutionary side of economic change; emergency and personality are its accidental side; and the whole result is incidental.

The question arises, what is to be said of the case when there is no legislation, or when legislation is repealed; in other words, of 'free' trade or enterprise or other activity. For nearly a century this was one of the chief issues which, in retrospect, gave a name or a nickname to the economic system of this country. Do free trade or enterprise mean that, so far as they exist, there is no purpose or plan for that aspect of the economy? In the forties of last century free trade was often described by its authors as a plan, as it had been described by D'Argenson before them. It is possible to make a distinction between policies and plans, which imply different degrees of intervention, and considered opinions which do not lead to any intervention. The free part of the economy can then be made purposeful by *consideration of the alternative*. Since the first Reform Bill it was on this consideration that the adoption and maintenance of free trade and free enterprise rested; they were both challenged by special critical movements of Protection and Socialism, the free trade issue having on two occasions been a direct political question. There is no policy or plan if a thing is not thought about at all,

but the adoption of a free system by consideration of the alternative is a different thing from neglect of that part of the economy or of its relation to the economy as a whole. The purposiveness of any free part of the economy is made more plain when it has not always been free, and a restriction or control is definitely taken off. Free trade was a clear instance of this. If, as in 1946, the government declares that it will nationalize some industries and will not nationalize others; or if at any time it protects some industries and not others; then the free part of the economy coexists with its considered alternative, which for it has been rejected.

Free enterprise is neither a policy nor a plan, since both of these imply some public control. But it is a system of the interacting personal purposive decisions of enterprisers, based on their estimates of the actions of each other, with the increasing help of public and private information of the market and of numerous methods of conference between themselves. Free trade and protection do not interfere with this *system*, they only affect the conditions of price or competition which enter into the estimates of enterprisers.

Of course, the free or private economy can have its own policies or plans. But when we are speaking of the national economy we distinguish free enterprise from the sphere in which there is a public policy or plan. A policy is directive; a plan is executive. A policy goes as far as to use some *instrument* which will influence the efforts of private agents. A tariff, or the rate of interest, a tax, a subsidy, or a guarantee, are such instruments of policy. It is only the instrument that is controlled. A plan goes beyond the instrumental stage; it organises the sphere to which it applies. That means some degree of public control over the *operation* of trade

or industry. There is interference either in industry or with industry; in industry, when a public monopoly is created, or public representatives sit on boards, or boards are publicly appointed; with industry, when public approval is required for private schemes. How far policies and plans differ from the framework of the law is a question of the time. Early legislation, as regards, for instance, factory employment or trade union activity, would then be called a policy or plan; but old plans become absorbed into the framework of law, and planning then means a new step in public control. Special cases of this are those activities which have always been reserved for the government, such as the currency and the mails; because of their antiquity we hardly think of them as now parts of the planned economy.

It should now be taken as a sign of a weak argumentative position when reference has to be made to the language in which early writers defended the free economy as a providential plan. This was the idea of last resort for writers who did not perceive the extent to which independent private agents act with conscious reference to what they expect others to do, so that these writers had to find some co-ordinating influence. It should be remembered that this providential attitude was adopted at that time in nearly every branch of thought, as an explanation of various kinds of harmonious arrangement and adaptation, and was not peculiar to economics. Also that providential control over human affairs is still very widely professed in general, provided it is not applied to any particular cases. It is not true that Smith said that an invisible hand harmonized public and private interests; no writer more strongly emphasized the opposition between the interests of certain classes,

and the public interest than he did. 'The clamour and sophistry of merchants and manufacturers easily persuade (the other classes) that the private interest of a part, and of a subordinate part, of the society, is the general interest of the whole'. 'Conspiracy against the public', by 'levying an absurd tax on the rest of their fellow citizens', was the practice of these interests. He allowed that there were 'many cases' in which private policy coincided with the public interest, implying that there were many in which it did not so coincide; it was to the former only that he applied his over-worked phrase, and he mentioned only one. The King's speech to Parliament still ends with an appeal to providence to guide the plans which it proposes.

When the presumption about a divine control is expressed without capital letters, it becomes the doctrine of the 'natural order', which early economists in England took over from the French school. This doctrine is the cause of much early confusion, and it was in conflict with the more particularly English doctrine of the greatest happiness which was first started by Smith's own teacher Hutcheson, and which Smith himself expressed. The utilitarian, or empirical, method had to release itself from the trammels of the abstract principle, and it did this, even at early stages, to an extent that is not generally appreciated.

There was, quite necessarily, as the national economy developed, a general question as to how far government should legislate on economic affairs; and the development of government itself, in representativeness and efficiency, was a factor in this problem. The government of Smith's time was very different from that of Mill's time or our time. This general question came to be argued by economic writers on the basis of the

utilitarian formula. But, since the economy of the nineteenth century began as a private economy, the burden of proof was placed on those who desired to increase public intervention; had we started with some kind of socialist economy, the burden of proof would have been on the relaxation of public controls, as it was in the particular case of the freedom of trade.

The change of government and of the economic system implies change in the meaning of words. Bentham said that 'security and freedom' were all that was required of government; and, after a century and a half, 'social security in a free society' is actually the motto of progress. When Smith gave protection as one of the three duties of government he could not foresee how far the 'protection of every member of the society from the injustice or oppression of every other member of it' would carry economic policy.

Smith never brought together his list of desirable public controls over private affairs, or of opposing interests in the national economy, or of defects in private relationships. Hence his scattered remarks on the opposed interests of masters and workmen; on rents and profits at the cost of wages; on apprenticeship against the public interest; on mercantile and other monopolies; on truck; on regulation of prices of necessities; on differential taxation; on education and public health; on public works; and on the priority of defence over opulence; are less well known than a few of the phrases in which he fell back on the presumption of personal freedom.¹ It was in opposition to two plans—the mercantilist and the physiocratic—which he thought were

¹ v. Viner, in *Adam Smith* (University of Chicago Press, 1928).

biased in favour of the town or the country, that he set the natural system of favouring neither at the expense of the other, by a reasoned argument. His 'common sense' is more often than not shown in his utilitarian tests, as when he says that 'all constitutions of government are valued only in proportion as they tend to the happiness of those who live under them'.

Two of his statements of policy require special comment. He said that the maintenance of public works was a duty of government; and his list of such works included all that at that time could have been possibly socialized—roads, canals, bridges, harbours, etc. Private enterprise could not be expected to erect or maintain these services, and this was a limited sort of socialism; but, at his time, the reservation to government, central or local, of any such functions was noteworthy. Second, his concessions to Protectionism went very far. The doctrine of defence as prior to opulence was not stated only in respect of the Navigation Act: 'if any particular manufacture was necessary for the defence of the society it might not always be prudent to depend upon our neighbours for the supply; and, if such manufacture could not otherwise be supported at home, it might not be unreasonable that all the other branches of industry should be taxed in order to support it'.¹ This goes a long way with modern Protectionism. And there is more than this. The one case in which he referred to the 'invisible hand' was that in which private persons preferred the home trade to the foreign trade, and he held that such preference was in the national interest, since it replaced two domestic capitals while the foreign trade replaced only one. The argument of the two capitals was a bad one, since it is the amount of

¹ Bk. iv, ch. v.

capital that matters, not its subdivision; but the invisible sanction was given to a Protectionist idea, not for defence but for employment. It is not surprising that Smith was often quoted in Parliament in support of Protection. His background, like ours today, was private enterprise; but any dogma of non-intervention by government has to make heavy weather in *The Wealth of Nations*.

Perhaps that is why the liberal system of thought was more usually referred to Bentham than to Smith. Though Smith was very often, and Bentham hardly ever, quoted in Parliament, it is Benthamism that defines the system in economic and social literature. His utilitarian formula is empirical; it does not depend on presumptions about 'rights' or providential control; as empirical as was the application of it in the middle range of last century. The 'greatest happiness of the greatest number' is an invitation to a continuous review of economic policy; and the greatest number is always the working classes. He distinguished between the agenda of government and the non-agenda. The wealth of the nation had three purposes, those of subsistence, security, and enjoyment, in that order of importance. And the agenda of government were the 'operations conducive either to the increase of the national stock in the matter of wealth, or to the application of it, in the most efficient mode, to any of its three uses, subsistence, security, and enjoyment, and which are not to be expected to be performed by the spontaneous exertions of individuals'. It was right to curtail enjoyment in the interest of the other purposes. 'Individuals may find their profit in commercial operations which may be opposed to the subsistence of all or the defence of all.' The private economy may be defective in respect of inclination, or power, or

knowledge, to act in the best way; then 'it is by the supply of the requisites so wanting that the action of government may display itself'. But 'without some special reason' for departing from it, the 'general rule' is private activity. 'Whatever measures cannot be justified as exceptions to the rule "Be Quiet" are non-agenda on the part of the government.' He proceeds to examine a list of non-agenda, which includes most of the usual restrictions on trade, and justifies them by the test of his empirical calculus.¹ As his economic Manual was written before 1798 it does not give an opinion on such events as the early Factory Acts or the Combination Acts. In the period called by Dicey the Benthamite period of legislation, from 1832 to 1875, his calculus was applied by Parliament so as to result in free trade, factory acts, company and trade union laws, enclosure acts, settlement acts, and land acts, but with many non-agenda that later became agenda, which is always the case with history.

These were the two who, by the understanding or misunderstanding of their whole doctrines, had the chief influence on public opinion before Mill. Ricardo and Malthus did not count for so much. Ricardo had no philosophical presumptions; outside his work on finance he had little to say on policy because he wrote a thought-book rather than a fact-book. He was a *reasoned* supporter of free trade; 'The *reasoning* by which the liberty of trade is supported is so powerful that it is daily obtaining converts'; but agriculture should be protected by a fixed corn duty to counteract its special costs. He supported the repeal of the Combination Act, to make wage-bargaining free. Ricardian socialism was based on a misreading of his theory of value, of

¹ *Manual of Political Economy*, ch. 1-3.

which utility was the 'first foundation' but not the relative measure. Malthus had many functions for government; to educate the citizens, give medical aid to the poor, assist emigration, protect children in factories, assist large families, protect agriculture, and sub-divide large estates.

The issue of public intervention was made sharper by two other writers, McCulloch and Senior. 'Government', said McCulloch, 'must frequently engage itself, or authorise individuals or associations to engage, in various sorts of undertakings affecting the rights and interests of others and of society'; it 'must not rest satisfied' with mere security and freedom of employment. 'It will fail of its duty if it do not exert itself to prevent that confusion and disorder in the distribution of property, and in the promotion of industrial employments, that would either not be promoted without its interference, or not so easily or completely.' 'It cannot, however, be too strongly impressed upon those in authority that non-interference should be the leading principle of their policy, and interference the exception only; and that no interference should ever be made on any speculative or doubtful grounds, but only when its necessity is apparent, or when it can clearly be made out that it will be productive of public advantage. . . . But, as long as this is the case, they should never hesitate in their course. It is the duty of the legislator, having once fully satisfied himself of the expediency of any policy, resolutely to carry it into effect.' He would have interference, at that time, stop short of nationalization; regulation and supervision should be enough. He was a strong supporter of the Factory Acts, of legislation for public health, and of free trade.

Senior insisted that economic science was a limited

study since wealth was only a part of welfare. It could only state 'general principles which it is fatal to neglect, but neither advisable, nor perhaps practicable, to use as the sole, or even the principal guides in the actual conduct of affairs'. Neither 'reverence for existing institutions', nor 'love of system', should deter an economist from stating the facts within his own sphere, or from drawing legitimate conclusions from them. But policy was for the statesman, on wider grounds than wealth alone. 'Many political writers', he said later, 'have supposed that public intervention should not be made, that the business of government is simply to afford protection. This proposition I cannot admit. The only rational foundation of government is expediency, the general benefit of the community. It is the duty of government to do whatever is conducive to the welfare of the governed. The most fatal of all errors would be the general admission that a government has no right to interfere for any purpose except the purpose of affording protection.' At different times he supported, on the principle of expediency, public works for the increase of productivity, assistance to emigration, combination of farms, measures for the relief of some manufactures, factory acts for children, and housing reforms; and opposed factory acts for men and women, the Combination Law of 1799, and the methods of the trade unions of his time. Whether the Poor Law of 1834, for which he was largely responsible, was an 'interference' or a 'piece of Benthamism', is a question on which, as we have seen, different views have been taken.

Mill distinguished between the necessary and the optional functions of government. Since his test for public interference is 'general expediency', this distinction is far from clear. Like Bentham, he offers a reasoned

argument against a number of 'false theories' of public policy, which include Protection, price-fixing, monopolies, and laws against trade unions. On the other hand, he thinks that 'all varieties of socialism' have a just claim to be tried, and that 'it is for experience to determine how far or how soon any one or more of the possible systems of community of property will be fitted to substitute itself for the organization of industry based on private ownership'. But he thinks that the defects of private industry, on which he speaks very strongly at his time, are capable of remedy, and he retains a presumption for private industry because of its educative value, because government was (at that time) a bad agent for industrial direction, because authority could be overdone, and because government could be overburdened for its necessary work. His presumption is shown in his general statement that public interference cannot be limited 'by any general rule except the simple and vague one that it should never be admitted but when the case of expediency is *strong*'. Yet 'in the particular circumstances of a given age or nation there is scarcely anything really important to the general interest which it may not be desirable or even necessary that the government should take upon itself, not because private individuals cannot effectually perform it, but because they will not', and in this connection he mentions certain public works. He was willing to have public factories and services in competition with private ones. In the House of Commons, in 1868, he replied angrily to the view of Mr. Lowe that Political Economy embodied an absolute set of rules. 'So far from being a set of maxims or rules, to be applied without regard to times, places, or circumstances, the function of Political Economy is to find the rules which ought to govern any

state of circumstances, which are never the same in any two cases. I do not know in Political Economy a single practical rule that must be applicable to all cases.' Even as a free trader he supported the defence argument of Adam Smith, and the 'infant industries' argument.

The next important economist was Jevons. In respect of public interference he defines himself as an experimentalist. 'We cannot plan out social reform on theoretical grounds. General arguments and information of all kinds may properly be employed in designing and choosing the best experiments, but specific experience on a limited scale and in closely proximate circumstances is the only sure guide.' 'Prove all things; hold fast that which is good'. 'In large classes of legislative affairs there is nothing to prevent our making direct experiments on the living social organism. Social progress is social experimentation, and vice versa. Legislation should observe the order of nature, and proceed tentatively.' He was, therefore, in favour, on the evidence, of the nationalization of the telegraphs, and against it for the railways. 'We cannot help speaking of principles and rights; they are only complex propositions founded on extensive experience, and indicating the probable results of actions.' In the case of the Factory Acts 'the presumption of good (in non-interference) was altogether rebutted by the certainty of evil'. 'No abstract principle and no absolute rule can guide us in determining what kinds of industrial enterprise the state should undertake, and what it should not. Nothing but experience and argument from experience can in most cases determine whether the community will be best served by its collective state action or by trusting to private self-interest'.¹

¹ *Methods of Social Reform (passim)*.

Jevons was a free-trader; he was also one of the first economic planners, in respect of the conservation and use of our coal resources.

At the end of the century came Sidgwick and Marshall. A large part of Sidgwick's argument concerns only those functions of government about which there has ceased to be any dispute, currency, coinage, defence, education, and so forth. His general conclusion is that 'the general presumption is not in favour of leaving industry altogether to private enterprise, but is in favour of supplementing and controlling such enterprise in various ways by the collective action of the community'. It is more difficult to place Marshall's views. His new definition of *laissez-faire* has been already referred to: 'Let the State be up and doing.' But this is not worked out, beyond some suggestions about taxation for urban improvements, and he distrusted even the municipal undertakings which had grown up. 'There is' he said, 'a strong *prima facie* case for fearing that the collective ownership of the means of production would deaden the energies of mankind and arrest economic progress; unless before its introduction the whole people had acquired a power of unselfish devotion to the public good.' 'If we can have "industrial chivalry" we shall not', he said, 'need socialism', although only then would socialism be feasible. On the other hand, he was the first economist to offer a rigorous proof that the price system of the free market did not result in the maximum of welfare, for which purpose government could interfere by the discriminating use of taxation and subsidy. That point is not important in socialist argument. Marshall banked heavily on the growth of moral sense in an educated community, and any concessions he made to the possibilities of collectivism were grudging. He wrote

as if he perceived the collectivist tendency, and wished to put a brake on it.

This review may serve to show how much truth there is in the contention that the nineteenth century was influenced by an economic dogma of non-interference. It was their almost unanimous support of free trade which led to a later reaction against economic writers. This was the standard case, from which the whole economy of the Victorian age derived its label. Yet in the whole debate of 1846 in both Houses of Parliament, laissez-faire was never mentioned, and the argument was based on positive issues and experiences; after that the purposive nature of the system was maintained by repeated consideration of the alternative. Other respects in which there was freedom accrued to give a name which was nearly a nickname to the period in which free trade was the dominant aspect. And the restoration of Protection in 1932 had a strong influence in favour of other forms of control, even if Protectionists did not mean it so to act. The special meaning of Protection, when it was adopted, made the way easier for more general meanings, and for other kinds of public interference or control. It was in 1932, as the result of the new trade policy, rather than in 1920, as the result of war, that the course of thought was changed, even among the economists.

CHAPTER 4

EFFECTUAL DEMAND AND EMPLOYMENT

The idea of enterprise is now applied to the public as well as to the private sphere. Besides its own requirements of enterprise, the public authority has by stages become an instrument of compensatory action in the interest of employment. This has had three degrees, ending in the doctrine of full employment in a sellers' market for labour. This doctrine is associated with a 'new economics' of income and investment of savings. But these ideas have had a long history in economic thought and should be regarded as the end of an evolution, without an artificial and inaccurate contrast with the ideas of classical economics.

WE have seen that a new interpretation of laissez-faire has been suggested by Marshall and Keynes, when they gave to that phrase the meaning that the State should be 'up and doing' in respect of those functions which belong properly to the public side of the national economy. That is to say, there should be efficient public enterprise as well as efficient private enterprise. This means several things. First, that the idea of enterprise belongs to the public side of the economy, which should therefore not be regarded as merely an administration of a limited function; it is only recently that the phrase 'public enterprise' has been given this new status. Second, that in the exercise of those functions which belong specially to the public sphere, and which would not be done at all if a public authority did not exercise them, there should be initiative and experiment in methods for the sake of economy and efficiency. Third, that in respect of functions taken over by a public

authority from a private one, the stimulus to initiative and enterprise which was given by competition should be provided by other methods of costing, accounting, or criticism. Lastly that, according to the stage which the whole national economy has reached in its domestic and international arrangements, public authorities shall be as active as private ones in promoting the extension of the service of each of their spheres of activity. The functions which 'properly belong' to public authorities may fail in development for want of any of these aspects of enterprise. But, as has been said earlier in this book, it is too paradoxical and unhistorical to call public enterprise by the name of *laissez-faire* applied to the State.

More recently, what 'properly belongs' to the public sphere has taken a further meaning. This is, that the State should be ready to act as a resource of last resort against defects occurring in the private economy, so that public policies should seek to be compensatory of these defects. There have been marked stages in the use of this idea. In the inter-war period, it was proposed that accumulated defects should be made good by a one-time extension of public work, which would place the economy on its feet again, and enable it to proceed thereafter by its own resources; although the defects were not all due to the private economy, they showed themselves there in unemployment and restricted output. Then there was the more continuous but intermittent proposal that the work of public authorities should be as far as possible retarded or accelerated, according to the general state of trade, being so to speak 'on tap' for this compensatory function. Lastly, because of the problems which this second method created, has come the proposal that, not public works alone, but a number

of methods of public expenditure, on either public or private developments, should always be ready for this compensatory action. It is obvious that some distinction has come to exist between normal and special functions of the State in relation to industry. This distinction might be overcome to some degree if it is argued that the private economy is so constantly liable to imperfection in its activity that it is almost a normal public function to be always ready to intervene in the interest of regular employment and activity. If there is a normal tendency for the trade cycle to recur, and this depends on its fundamental explanation, it is a normal public function to anticipate and prevent it; and this is compensatory of private activities in industry and trade only so far as the defects arise there. But the larger the sphere of public industry, the more possible is it that the defect may arise from insufficient or faulty enterprise on either the public or the private side. A part therefore of such public expenditure may be strictly 'compensatory', and a part arise out of conditions in the public sphere itself.

In this country, and in many others, a considerable part of employment and production is in the hands, or under the auspices of public bodies. How far public employment and production go beyond the necessary minimum of the duties which *must* so be taken, is a matter of history. In this country, many services have come to be transferred from private to public authorities, especially local authorities; and the nationalization of fundamental industries has begun to increase this tendency. It has been estimated that, in the inter-war period, about a third of the national income was spent by public employers; a century ago, it was about a seventh. The industries and services which are most

suitable for public administration have hitherto been chosen for their fundamental relation to local or general private industry; private industry therefore depends in a special degree on the enterprise and efficiency with which the public sphere meets the needs of a growing population, and offers the most suitable conditions for private industry. Before they became public, these occupations had to do their jobs as producers and employers, and their transfer to public hands does not change their relation to the whole field of production and employment. The requirements of private enterprise become requirements of public enterprise; and defect of enterprise will have the same result in either case. If public enterprise is not up to date, its demand for goods, materials, and labour will not sustain incomes and employment, and this will have the same effect on the activity of trade and industry as a similar defect anywhere else; or, if anything, a greater effect, because of the fundamental nature of what they have to supply as a basis for the development of private industry. Public industries have some power, which private industries do not have, to maintain their employment against depression, since they can make the consumer pay in rates or taxes, or in the protection of their activity, open or disguised. But a defect of enterprise, public or private, means insufficient development of initiative, invention, or foresight; and, if this defect arises on the public side, the loss of employment will show itself mainly in its effect on private industry. Private industry is therefore liable to be charged with failures of employment, which lead to an argument for a greater development of public industry, though the problem may have begun in the latter. The mutual support of employment, production, and income depends on the whole

field of enterprise, public and private. The more extensive and fundamental are the occupations in public hands, the greater is their requirement of enterprise.

The relation of public to private enterprise has been inquired into both as a normal one, and where there have been abnormal conditions. We can go back to Say and Adam Smith for mention of the public activities which should be always undertaken to 'facilitate commerce'. Between the two wars of this century, there were inquiries which listed the activities of public authorities which were suitable for further development to meet the unemployment of the depression of 1931-2. If we strike out of this recent list the industries or services, such as electrification, or telephone development, which did not exist in 1800; or agriculture, whose position then needed no development; we are reduced to roads, bridges, canals, and harbours, which are precisely the list of Say and Smith. They stated all that they could then have stated of the modern list of normal public enterprise. The extension of the list of normal public enterprises has been due to the growth of local services which have a special relation to the use of the public domain, their fixed capital being coextensive with their market, and which, being thus naturally monopolistic, have been transferred to municipalities. In 1931, public services employed about one-tenth of the employed population. In 1946, the Socialist government gave a ratio of 20 per cent of public to private service as a suitable equilibrium,¹ which may be compared with Mill's statement a century earlier, that private enterprise should be the general rule. Public enterprise is often taken as the same as 'planning', while

¹ This ratio had been reached in 1949.

private enterprise is taken as one of the senses of *laissez-faire*. The normal relation now proposed may be said to differ from Mill's in that the general rule has been defined.

Whatever proportion may at any time be normal, the point is that the whole of the field of production, income, and employment includes these two sides, and that a good economy depends on each side being fully enterprising and efficient. The same would be true if we made any other cross section of the whole field, for example, by distinguishing between the 'consumption' and the 'investment' sides, or between the 'agricultural' and the 'industrial'. The ideal is, that we should not have to create a special development on either side only in order to compensate an abnormal position on the other side. The second best is that such compensatory action is possible to meet unforeseen emergencies arising on either side, especially if the forced adjustment acts more favourably on one aspect of welfare, namely employment, than it acts unfavourably on another aspect, namely real value of production. The difference between the cross-section into public and private enterprise, and any other cross section, is, that public authorities can *confidently* undertake special developments, since they can assure the cost of them out of rates and taxes, and it is defects of confidence in the market which cause private recovery to be most hesitant.

The compensatory function of public enterprise has had a number of phases. The first to notice is compensation for the effects of its deficiency. It may be behind its own normal development, in relation to the rest of the economy, either by want of enterprise or by the unavoidable results of destruction by war, or some

other impediment. Between 1929 and 1935 a sharp controversy arose on this issue, initiated by Mr. Lloyd George, and carried on in a series of pamphlets, to which the government contributed.¹ The essence of the argument was, that the extreme depression which had occurred was also an opportunity, because there were serious arrears on many sides of national development. The country was said to be backward in respect of roads, bridges, drainage of land, electrification, telephones, canals, and the improvement of the countryside; all of these being functions of public bodies. So that 'this period of wide and prolonged slackness and unemployment offers the best opportunity ever presented to us as a nation for setting right many things we neglected in periods of prosperity'. Obviously, such defects in public enterprise were bound to embarrass private industry, as was admitted; 'there is a limit to what private enterprise can accomplish unaided'.² A 'great constructive effort' was to be made, involving the expenditure of about £250 million over a limited time, in order to destroy the 'hard core' of what was regarded as exceptional unemployment. The authors of the private pamphlets thought that, once the special depression had been remedied by a special public effort to make up leeway, once the patient had 'turned the corner', the relations of public and private enterprise would become normal again, and private industry would then proceed 'under its own steam';³ the normal figure of unemployment being that which prevailed before 1914, an average of about $4\frac{1}{2}$ per cent. There was substance in the official reply of the Treasury that a special outburst of public

¹ See the Bibliography.

² *Organising Prosperity*, 1935.

³ *Can Lloyd George Do It?*, pp. 8, 14.

activity only postponed the general question of the continuous relation of public to private enterprise. In this debate, the distinction was made clear between a minimum (or normal) amount of unemployment and the cyclical extra unemployment which had periodically recurred. The remedy for the latter was to be found in many methods of increasing the efficiency of industry, and removing restrictions. It was at any rate a very insurable quantity. It was the urgency of special unemployment which dominated the question at that time. The very defects in the framework of the economic system which were set forth became themselves a solution, because their magnitude itself made room for a large absorption of unemployment. Of course, 'crisis action' of government might recur, and this would be the minimum form of unemployment policy.

An advance on the one-time proposal is that of the intermittent compensatory function of public enterprise. As will be seen, this idea goes back to such early economists as Steuart and Say, but did not enter the field of policy until 1909. It could hardly do so until the scope of public enterprise had been extended by the municipalization of local services. The normal development of public work depends very largely on the growth and distribution of population. It is for that reason that there are difficulties in the idea of the compensatory acceleration or retardation of the work of public authorities, and in the relating of their activity to something which does not vary with population, namely, the activity of trade in general. This idea, an intermittent relation of public to private enterprise, was brought into a high focus in the Reports of the Poor Law Commission in 1909. The pamphlet of 1929-35 might be interpreted as having it in view when they spoke of industry,

after the special effort they urged, proceeding 'under its own steam' with what might be regarded as a normally compensating engine for cyclical changes.

The Reports of the Poor Law Commission, and of many subsequent arguments which took the same idea of the 'regularization of the demand' for labour, was that public and private enterprise were placed in the same sort of relation to each other as Gladstone's 'two attractive sisters' in the days when taxation was the instrument of policy; both being the children, as he said, of Necessity and Invention, but taking after different parents. But in spite of the prominence given to their mutual relationship in 1909, and in economic discussion, it was stated in the most important of the contributions to the debate of 1929-35 that this form of the idea of compensatory public activity had 'never been seriously put into practice'.¹

No evidence was taken by the Poor Law Commission from the public officials who would have to administer this plan, namely the City Engineers. Their argument was of a general form, except for a statistical statement of what, in retrospect, could have happened over a decade if the plan had been applied with knowledge of the future. But the administrative problem of public officials was, that they were asked to reserve contracts of public work against a slack time of unknown date. If it is a cause of unemployment that resources are not spent or invested, they were being asked at times to do

¹ Under the Public Works Act, 1863, local authorities in manufacturing districts could borrow for works of permanent local advantage, in order to relieve unemployment. About 1½ millions were borrowed mainly in Lancashire, to relieve the cotton famine, the maximum number employed at any time being about 6,500. (W. O. Henderson in *Economic History* No. 6.)

that very thing; and if all local authorities acted so, the effect on the market for labour might be greater than they could foresee. It is no use breaking the market in order to repair it. Further, there may be public contracts of such a kind that the amount of labour needed for initial construction is not great in relation to the amount of labour needed to operate after construction; and other contracts may be of the opposite kind, so that they need much labour to equip and start, and much less to operate. In order to fit public employment to the time when it could be most compensatory, a difficult decision between these two sorts of contract would be required, and public officials could not be expected to make it. The majority of the Poor Law Commission held that it would be 'pernicious' to cure irregularity of the market by deliberately making necessary public work more irregular, but vaguely held that 'irregular' contracts could be adapted; the Minority were bolder, but both sides spoke with great generality on the subject. The proposal remained economically feasible as an argument, but it was administratively difficult. In addition, local government in this country is run on party lines, and unpopularity may be incurred by 'reserving' a municipal extension or development.

If there is slackness in the demand for labour, the thing most needed is to find its cause; and there may be other methods of dealing with that than forcing public contracts to take the strain, while the real cause is not attacked. The case may be one for fiscal or currency and banking policy, or subsidies, or action against restrictive practices all of which could not be blanketed by 'public works'.

This is the difference that is now made by a third method, the proposal to create a *constant* 'sellers' market

for labour'. The idea of a sellers' market first occurred in the work of Malthus. His plan was to keep the population within the means of subsistence; 'one objection which will perhaps be made to this plan is that from which alone it derives its value—a market rather understocked with labour'. This idea was continuous in the economic attitude toward the population question during the nineteenth century, and persists in subsidiary proposals for scarcifying labour by raising the school age, or enabling old persons to retire from work. But the argument of the Beveridge policy is independent of the problem of population. The sellers' market for labour is to be got by the elasticity of the public methods for increasing or maintaining the public and private demands for the labour of any population. This will not be done by public works alone; other methods are also to be used for stimulating private investment or consumption. The essential point is the continuity of supervision over the actual or expected course of trade, and this is its difference from the intermittent policies which had till then been the chief suggested resource. Besides its greater continuity, it has a greater centralization than a policy which was scattered over a number of local authorities. It assumes that, in a developing nation, there can be useful work for all disposable labour, if the mutual interactions of spending and earning do not fail for want of confidence, and if the interval between saving and investment, due to the division of these functions, is bridged fast enough to maintain the income out of which both saving and investment, and therefore employment, come.

The aspect of public or private industry for which public policy is to be made a remedy, is the trade cycle.

The existence of this tide in the economic affairs of men was perceived and was a frequent matter of Parliamentary notice as early as the end of the eighteenth century. No theory of it could exist until it had recurred often enough to deserve the name it received late in the nineteenth century, when the problem of the cycle took the place of the problem of 'crises'. And the most important of the many aspects of the cycle was the fluctuation of the rate of unemployment, through which the study of the cycle was linked with proposals for compensatory public works or activities.

The trade cycle, as its name implies, is something more than the arithmetical fact that any historical statistics have an average or line of trend, about which they vary. The statistics of, for example, shipwrecks have such a variation, but it is quite irregular, and would not be described as a fluctuation. Fluctuation means four things. First, that between a high turning point and a low one the direction of change is continuous; second, that between such points the movement crosses the base or trend line; third, that the curves drawn between the successive high points and the similar low points (the envelopes of the cycle) show the movement of the amplitude of the fluctuation; lastly, that there is some degree or regularity in the interval between successive high or low points. It is because the indices of prices, employment, production and new investment (as shown by company formations), meet these tests that the problem of trade cycle studies exist.¹ It would be possible to have a purely theoretical study of a trade cycle if none had ever existed (and some studies approach this form) but history has set the problem of why it has existed.

The period over which this fluctuation has existed is

¹ v. my *Enterprise, Purpose and Profit*, ch. 3.

so long that it covers very great changes in the form of the national economy, from a life mainly agricultural to a life mainly industrial, and from low forms of industrial organization to high forms. Therefore the cause is naturally sought in economic influences which prevail at all times, and the most fundamental of these would be, any constant aspects of the nature of economic man, and physical conditions. These are the two poles of the economic question. Hence, if the trade cycle was not due to a series of different causes at nevertheless fairly regular intervals, but was one problem, its historical range suggested either a psychological or an agricultural explanation.

Since the middle of last century, there has been a continuous reference in economic literature to the psychology of the private market in explanation of the cycle. Traders became more or less hopeful, or more or less tired. These were called 'moral causes', or 'a normal tendency of the human mind', by writers in 1857 and 1867. The outward sign of these influences was the condition of credit, or of business confidence. Later, it was called optimism or pessimism. Marshall adopted this view in 1879, and Pareto in 1886. Pareto thought that this 'general law of rhythm', ruled 'all social phenomena', and applied to other forms of human endeavour as well as to those of business. Pigou resumed the theory in this century, and Stamp concluded later that 'if all other national elements in economics were entirely stable, it is probable that the human element is itself rhythmic'. Others who wrote to the same effect include Juglar, Overstone, and Guyot. Hawtrey's 'instability of credit' means the same thing, since the state of credit was taken by others also as the outward sign of the psychology of the market. The income

analysis of more recent times also leads back to the same problem, since there must be some want of confidence to explain why the nation does not spend in one way or another what has become income.

The other pole of the whole economic system is the physical conditions of supply, hence the reference to harvests and to weather cycles as a fundamental cause of the fluctuation of private activity. This would act through changes in the purchasing power of agricultural countries, and agriculture is much the largest industry in the world. A fall in their purchasing power would affect the export trade of manufacturing countries, and the influence on employment would spread. It has been held that there is such a natural rhythm in agricultural production.

The explanation of the recurrent cycle is not that these two kinds of rhythm coincide, when they might have modified each other. Physical changes only affect trade through the reactions of persons to them. The distinction is between an autonomous tendency to rhythm, such as Pareto and Stamp have supposed, and an induced tendency. Any cause must act through the psychology of economic agents, even if it does not start there. The control of the cycle has to dose that psychology, and the theory now on trial is like the discovery of a medicine for reducing its worst effects. If there are physical causes of a fall in production, public policy cannot always make up the deficiency in real income, but it is claimed, as seen below, that a deficiency in employment need not follow. While if the rhythm is purely a matter of an ebb and flow of enterprise, public policy can shift the emphasis of enterprise from private agents liable to this psychology to public agents not so liable, or the emphasis of consumption from those who

save to those who spend. This statement covers many wheels within wheels, but it defines generally the relation now sought between the public and private sides of the whole economy. That relation is not the ideal one, since public enterprise has its own work to do; but it is now almost normal. It has to avoid creating in the private market a new psychology of dependence on public plans.

The new proposals are different from the 1909 idea of keeping public work on tap against fluctuation. They go further, in respect of the investment to be used. It is not only public investment that is to be handled; there is to be assistance to revival of private investment, adjustment of taxation so that it will fall more on those who save and less on those who must spend, government purchase in bulk and, if necessary, nationalization. But public investment or expenditure has the largest place. In the 'man-power Budget', it is the duty of the Minister 'after estimating' the prospects of all investment, to propose outlay sufficient to employ all the available labour, and to raise it as far as possible by taxation'. Of course, this is no more than a statement of the problem; the meaning is, that full employment will be possible if he is able to propose and provide for productive outlay of this amount. Employment for a threatened half-million of unemployed will require, on the estimate made in 1935 that £1 million would employ 5,000 men for a year, schemes amounting to 100 millions always ready, or at least 150 million in post-war prices; and there must be a second such scheme in reserve for the next year in case it is required. Probably, there will be some strain on the meaning of the productiveness of the employment, and the employment aspect will take priority over other aspects. Indeed, supporters of the

new theory point out that the productivity is all to the good, but the employment is the essential thing. How far high real productivity can be obtained with full employment is the question of what Beveridge has rightly called the 'adventure' of this plan. The 1909 methods did not succeed, and something of wider range and more continuous application is to be tried. A 'sellers' market for labour' is a statement of the aim of the policy; it does not cut the knot without regard to the conditions of success. In this country, labour cannot be industrially employed without imported materials; the conditions on which we can get them are of the first importance. The 'adventure' has started with a post-war surfeit of things to do, and that is a good start; after this transition, and after the American help is exhausted, will be the time when our economy will face its fundamental problem of employing 20 million people in their location in these islands, with their necessities of import.

It may happen that for full employment the productive value of government work will have to be very broadly understood. Beveridge has laid stress on 'social priorities' in the interpretation of these results. It must always have been plain enough, as it was to Mill and others, that there could be full employment if employment was itself the first priority. The following quotations, almost repeating the same words, may be noted. 'Better it is to engage in works of ostentatious convenience . . . better would it be for the State to build pyramids or towers of Babel, than that those who have hands and are willing to work should hunger for want of employment.' This was written by Southey in 1812. 'The immediate effect upon employment of a scheme of investment is nothing whatever to do with the usefulness

or earning power of the capital goods produced. When the Tower of Babel was being built a large number of men were engaged on an entirely unproductive enterprise, but while they were at work they had to be clothed and fed; their wages were spent upon the current output of consumption goods industries, etc.' This was written in 1937.¹ A lengthy note in the well-known pamphlet of Spence in 1807 anticipates almost verbatim this last quotation, with the substitution for the Tower of Babel of the 'blowing of glass bubbles'.² Three main ideas of the national optimum have been set forth at different times in the greatest national dividend, the greatest welfare, and the greatest employment. We can seek to depend on the two former for the last of these, or we can go for it directly, in which case the middle idea of welfare will be an adaptable bridge between the other two. How far, in fact, is employment to be regarded as one of the things that industry is 'for'? It should be observed also that the substitute of some welfare for some wealth can be made without much prejudice to a public feeling of this kind, because even private consumption is full of elements of doubtful real value, though they contribute to employment. We obtain, in fact, a maxim of the 'greatest production by the greatest employment' as an economic reading of the utilitarian formula.

But, to return to the opening of this chapter, it is still best that public and private enterprise should each be so carried on that the Minister of Finance will find, when he makes his man-power estimate, that he has not to make any special compensatory expenditure, or the

¹ Joan Robinson: *Theory of Employment*, p. 33.

² *Britain Independent of Commerce*, pp. 74-7, pp. 36-7.

less the better. And this leads us to consider the contrast, set forth by Beveridge, between the rate of unemployment before 1914 and its rate after the first World War. The former averaged two-fifths of the latter. It is uncritical to leave that contrast without reflection upon it; the more so, if 3 per cent is, as Beveridge has said, a necessary average provision for immobility and some other things. If this were deducted from the pre-1914 average, we should be left with about 3 per cent of average avoidable unemployment. Yet Beveridge often speaks of this 3 per cent as a minimum, which implies a higher average. Waiving this point, there must have been aspects of the economic framework before 1914 which were favourable to high employment, and which we have lost. These were the days when the economic framework was based on free trade, private enterprise, the gold standard, low and slightly graduated taxation. If any of these, like the gold standard, was a drag on expansive enterprise, so much the better for the others. Public methods of maintaining expenditure now are not a complete substitute for all other considerations of the economic system, and it should not be assumed that all the methods forced upon us in the inter-war period are to retain their place.¹ The change of attitude about gold, debt, free trade and 'sound' finance, has a recent history of unconvincing completeness, as if argument had rather tired than concluded. Government should not have to undertake action which is compensatory of conditions which may be the result of policies which may themselves require to be reconsidered or revised; the resource of public schemes of investment or expenditure should not come to be a support for restrictions or defects

¹ W. H. Beveridge and others: v. *Tariffs; the Case Examined*, 1931.

which have remedies of their own, the neglect of which will throw too great a burden on the devising of public plans for maintaining really productive employment. We should not take 1938 as a datum line as regards the forced policies which had by then entered into our economy, upon the acceptance of which we are to build the further structure of public control over investment and expenditure. The economy which was broken in 1914 is not so obsolete as to have nothing to contribute to a judgement on the methods which kept the rate of unemployment at an average which in the inter-war period we would have been glad to recover. The largest aspect of this is the degree of free international trade which is still most necessary in the permanent nature of our economy. We are at the end of a generation which has seen forced changes in that economy, mainly as the result of war, and if peace is now to prevail we have historical reason, in the history of the fact of unemployment, to keep several questions open to review.

The question of public policy, as compensatory for a threatened fall in the private market, is different from the question of the nationalization of industry. It has been argued that, if the former policy is not fully successful in relation to employment, it will be necessary to consider the latter as a further step. This appears to mean that the State will be in a stronger position to act on employment in a nationalized industry than to do so by assistance to private investment, or by new public works. This is a very arguable contention, since transfer to public hands would not in itself prevent the supply of most commodities from being affected by general fluctuations in demand; and the compensation for this would be the same as if it had happened under private management. There would be no more reason in one

case rather than in the other for applying the compensatory action to that particular industry. If a nationalized industry has to pay its way, as it is required to do under the Coal Board, special expenditure upon it for reasons affecting employment as a whole would be prevented; while its own employment would still depend on the market. It would merely happen to be the case that among the things to be compensated by the general policy of investment, assistance and tax adjustments, there would be any fall in employment in nationalized as well as in private industries. A public monopoly can make an industry pay its way by price policy, but not so as also to maintain employment in the industry. Public policy, as remedial for unemployment, applies to investment, or assistance to investment, or fiscal measures, which are chargeable against the whole community in taxation, while it cannot force the consumer to maintain both employment and a balanced account for anything which depends on market prices. It is therefore too abrupt to say that, if the general policy is not fully successful, it might be necessary to nationalize some industries.

The developed phase of public policy which has been discussed is related directly to the economic theory of Keynes, which was expounded in 1936, and is known as the 'new economics'. It fastens on a phrase which had already been often used in economic thought, namely, the 'effectual demand'. The idea behind this phrase had also been implied in economic policy, both liberal and protectionist, each of which believed that more money would be available for spending, and would so maintain employment, if its methods were adopted. Such an implication was in fact inevitable.

But it was now disengaged from these implications, and was made the central idea of the new theory.

The fundamental propositions are these. First, the incomes of all people depend on the expenditure of other people. Second, if all the incomes are spent in one way or another, the whole income will be maintained, and also the employment which created it, if general prices are steady. Thirdly, money which individuals save must therefore re-enter the circulation by the borrowing and spending of other persons, public or private, failing which the whole income will fall. Fourth, there is a gap between saving and spending, since the saver is not the same person as the spender of borrowed money; this gap should therefore be quickly closed by the investment of savings. Fifth, if savings are invested, they will maintain both the income out of which they have come, and will themselves be exactly maintained so that the investment will in a sense be self-financed. The effectual demand of the nation will thus be maintained, but it will require a public intervener to do it, if private enterprise does not rapidly take up private savings. There must either be public investment, or policies to increase private enterprise or private consumption. Saving must be offset by some kind of spending, in order that full expenditure may maintain full employment, and vice versa. Idle savings limit the income they might have maintained, and clog the whole effectual demand.

It is necessary to distinguish between causation and analysis. If £1 million are invested, and if the community at the time saves a quarter of its income, that investment will *mean* an income of 4 millions, of which a quarter is saved, which is the investment itself. The period over which the investment takes place is also the period

within which the savings are being made; the 'rounds' of expenditure are not successive to the investment, they are an integral within the action of the investment. If savings and investments are equal as an identical proposition, they are not made equal as the result of a process, during which the savings catch up with the investment; for then the investment would be for a time ahead of the savings, and the identical proposition of Keynes would fail.

It was objected to the 'old economics' that it assumed certain coincidences between private and public interest through the agency of an invisible hand. Now, if it were true that, when some people invest for the sake only of their own gain, and others save for the same motive, but that in time the savings come out so as exactly to replace the investment, the invisible hand would be keeping its watch over old and new alike. But it needs no such supervision to maintain an identity.

We have now to consider how far the doctrine of the new policy is itself new. It is natural to make a taking-off point for later developments by critical reflection on what preceded them. This criticism has resulted in bringing into economic argument the hitherto neglected work of J. B. Say, because something called 'Say's Law' was chosen to be the model of what should not be believed. Say may now owe as much as Hobson to Keynes, who had studied Hobson closely, and some study of Say may come to be substituted for the present echo of hearsay.

'Say's law' is regarded as one form of the view that private enterprise can by itself maintain effectual demand as far as the complexity of the economic system allows. It is supposed to mean that all sellers are

necessarily buyers of either consumption or production goods, so that the value of sales at once supports that of purchases, which imply other sales, and this constant interaction maintains employment, covers cost, keeps production up to the level of effectual demand, and gives the fullest employment to be expected under complex and changing conditions of supply. These references to Say's law have not been accompanied by quotation, and they misrepresent that author, who could in fact be quoted in support of the more recent analysis. Say stated the general principle that 'it is production which opens a demand for products', because it creates by sales the funds to buy other products, and that traders are as a rule anxious to 'dispose of the money they get' quickly. 'It is an advantage that the successive operations should be rapidly executed', and 'every product, when completed, repays by its value the whole amount of productive agency employed in its completion'. He rejected the view of Malthus and Lauderdale 'that capital is by accumulation withdrawn from consumption'. 'Disposable capital will seldom remain unemployed; there is every reason to believe that as much industry will be called into activity as the actual state of society will admit.' But this general rule, he said, is liable to fail, when persons are not using their own capital. Stagnation may occur if traders 'have found difficulty in the employment of their productive resources', with the result that 'the value of products is less than the charges of their production, profits and wages decrease, the labouring classes experience a want of work, etc.' Therefore 'every industry is sometimes in circulation and sometimes not'. But *'no act of saving subtracts in the least from consumption provided the thing saved be reinvested or restored to productive employment. On the*

contrary it gives rise to a consumption perpetually renovated and recurring.'¹ 'It is an advantage that the successive operations performed in the course of production should be rapidly executed', and the title of this chapter is 'the benefits resulting from the brisk circulation of money and commodities'. 'Values once produced may be devoted either to the satisfaction of wants or to a further act of production. They may also be withdrawn both from unproductive consumption and from reproductive employment, and remain buried or concealed', the causes of this being some 'want of confidence'. In which case 'a benevolent administration can make provision for the employment of supplanted or inactive labour in the construction of works of public utility at the public expense, or in the transfer of population from one spot to another'. These statements, written 150 years ago, cover all that he said, and they read more like a prevision of what is now more fully considered than some 'law' from which, for the sake of contrast, we have to separate ourselves. Indeed, there is enough plainness in these ideas to account for their perception at early stages of economic thought.²

These references to the *Treatise* show that Say was aware of possible misfits between saving and consumption which it might require public investment to put right. There was an argument between him and Malthus on the nature of the problem. Malthus had argued that a failure of effective demand (that is, of demand which replaced costs of production) was always liable to occur if saving was out of proportion to expenditure.³

¹ This could be either Say's Law or Keynes' Law. Say, *Treatise*, bk. 1, ch. 11.

² The quotations from Say occur in ch. 7, 11, 15 and 16 of his *Treatise*, bk. 1, and ch. 2 of bk. 2.

³ *Principles*, bk. 2, ch. 1, *On the Progress of Wealth*.

Keynes regarded this chapter as a neglected basis of what might have been a better development of economic thought than actually took place.¹ It is in fact a loose, vague, and inconsistent chapter, which would be refuted by its own conclusions, even if Malthus had not in the end thrown in his hand, and allowed that the proportion of saving to consumption would be adjusted by 'natural' causes and private interests. He had argued that, if rich people did not have the will to spend, poor people did not have the power; and the remedy was not to give them a greater power of consumption, since that would put up wages, and discourage production; but to allow a place for 'unproductive consumers', who supplied no material goods, such as lawyers, doctors, and soldiers, and especially the rentiers of the national debt. If the country, he implied, became so healthy, law-abiding, and peaceful as to need fewer of such services, it would be in danger of gluts of production; and the national debt had a function in that the rentiers maintained demand. The taxpayer who supported the rentier was made more energetic by the fact of taxation; so that he really produced in place of the rentier, and where was the argument then? During the nineteenth century there was in this country a shift from primary to secondary, and then to tertiary industries; these last are among Malthus's unproductive consumers, but no one could contend that their relative increase was an influence against depression. Between a quarter and a third of the population are children and old people, which ought to be enough of unproductive consumption if this is what is wanted. Malthus had got the idea that only an influence *from outside* could keep industry active, and

¹ *Essays in Biography*, p. 144.

therefore, in another section of the same chapter, he argues that an increase of population will not by itself increase effective demand; for no one will employ it unless its product exceeds its own consumption, so that there must first be an outside demand for the excess. He is really bemused by the problem how any employment ever begins, and does not see that the new population goes into several industries each of which is outside the others, and that demand is reciprocal. Malthus was sensitive to the concept of effectual demand but, if this chapter of his *Principles* had been influential, it would have required someone like Say to restore the fibre of economic thought. It could not stand that what a nation needs for stability is taxes, debts, high money values, and unproductive consumers.

In his *Letters to Malthus*, Say shows many of the inconsistencies of Malthus's argument, both with itself, and with the Essay on Population. How can effective demand fail if population actually presses on increases of supply? How could demand fail by the 'indolence' of the consumer, in preferring leisure to goods, if also unproductive consumers were necessary to sustain demand? As for a general abstinence from consumption by the same people who went on saving, this was the same sort of problem as the moon falling on the earth. (Of course, at any time some are saving while others, or their families, are drawing on savings.) In these *Letters*, Say is concerned to emphasize the fundamental fact that what creates the power to buy is a large amount of employment, not of unemployed or non-productive persons; that the value of the product creates the power to buy the product; and that this is the governing principle on which policy should proceed. Surely it is just on these ideas

that modern analysis now bases the method for maintaining demand and employment.

Malthus had in the end abandoned his argument in concluding that 'whenever capital increases too fast the motive to accumulation diminishes, and there will be a natural tendency to spend more and save less', and that 'these tendencies, operating on individuals, direct them toward the just mean', so that 'in leaving the whole question of saving to the uninfluenced operation of individual interest we shall best conform to that great principle laid down by Adam Smith, that the wealth of nations is best secured by allowing every person to purchase his own interest in his own way'. While Say was one of the first to observe that public employment might be necessary to bridge the irregularities of the market.

Between money and commodities, Marx made a law of circulation expressed as $M-C-M$; while Say made a law in the order $C-M-C$. Perhaps this may be called his 'law'. But this order of proceedings is not in itself a law of effective demand, unless M is taken at the full-cost value of C in each direction. It is pressing Say too hard, as the quotations from the *Treatise* show, to suppose that he assumed this.

Sometimes 'Say's Law' is stated in a quotation from Mill.¹ 'All sellers are inevitably, and by the meaning of the word, buyers. Could we suddenly double the productive powers of the country . . . everybody would bring a double demand as well as supply; everybody would be able to buy twice as much because everyone would have twice as much to offer in exchange.'² This is strictly true of an individual transaction; a seller of

¹ v. Keynes, *General Theory*, p. 18.

² *Principles*, 3, 14, 2.

goods is then a buyer of money; or as a statement of ability to buy. It is to the failure to use this ability that Marshall refers in the same quotation from Mill. Say pointed out that the gap was liable to exist when people were not spending their own capital,¹ that is, in Keynes's words, when those who save are not the same as those who invest. This is, of course, an ordinary condition; but the quotation from Mill should be made complete. 'The demand which influences the price of commodities consists of the money offered for them. But the money offered is not the same thing with the money possessed. It is sometimes less, sometimes very much more. In the long run, indeed, the money which people lay out will be neither more nor less than the money which they have to lay out; but this is far from being the case at any given time. Sometimes they keep money by them *for fear of an emergency, or in expectation of a more advantageous opportunity for expending it.*'² And he proceeds later: 'There can never, it is said, be a want of buyers for all commodities; because whoever offers a commodity for sale desires to obtain a commodity in exchange for it, and is therefore a buyer by the mere fact of his being a seller. This argument is evidently founded on the supposition of a state of barter. When two persons perform an act of barter, each of them is at once a seller and buyer. If, however, we suppose that money is used, these propositions cease to be exactly true. *The buying and selling being now separated*, it may very well occur that there may be a very general inclination to defer all purchases as long as possible. Persons in general, at that particular time, liked better to possess money than any

¹ *Treatise*, bk. 1, ch. 11.

² *Principles*, bk. 3, 12, 2. These are two of Keynes's 'demands for money'.

other commodity.’¹ The result is periodic stagnation; and this follows from the same gap which Keynes and Say had observed, the division of functions, and the use of money.

Indeed, the most direct statement of these ideas had been made before Smith, Malthus, or Say, in the *Maxims* of the founder of the Physiocrats, Quesnay. These *Maxims* of government were published in 1758.² ‘The entire income of the nation should return into and permeate the annual circulation. Incomes should not be accumulated in money, since such accumulation retards the distribution of a part of the annual income of the nation, blocks the national savings, and prevents the replacement of loans to production, as well as the maintenance of wages and consumption’, and such interception of savings ‘lessens the continued production of incomes, and public revenue’. ‘Owners of property and those who follow profitable occupations should not make sterile savings which withdraw from circulation and distribution a part of their incomes or profits.’ ‘Government should be less concerned with economy than with the operations necessary to the national prosperity, provided extravagance is not mistaken for expenditure.’ These are just the ideas which a new economics had developed into a system, but it is the system not the ideas, which are new.

The first British economist to perceive the importance of maintaining effectual demand was Steuart, who came between the Physiocrats and Smith. He is not usually included among the ‘classical’ economists, although Say quotes him several times, and Marshall refers to him as one who made ‘important additions to economic theory’. He anticipated Smith and Malthus in the significance

¹ *Principles*, 3, 14, 2.

² *Oeuvres*, Oncken’s Edition, p. 328 *seq.*

as well as in the statement of effectual demand. 'It is the effectual demand, as I may call it, which makes the husbandman labour for the sake of the equivalent.' 'The demander must have an equivalent to give; it is this equivalent which is the spring of the whole machine.' And 'every transition of money from hand to hand for a valuable consideration implies some service done, something wrought by man, or some consumption of something produced by his labour. The quicker, therefore, the circulation of money is in any country, the more strongly may it be inferred that its inhabitants are laborious.' This doctrine of the equivalent is central to his *Inquiry*. 'My principal point in view is, to find out a method for enabling those to buy who at present cannot, because they can give no equivalent.' He holds it to be the duty of the statesman to maintain the circulation of money if it appears liable to stagnate, when the 'propensity of the rich to consume' is not in proportion to the 'disposition of the poor to be industrious'.

This distant echo of modern thought is heard also in respect of economic motive. 'Difficulty in selling labour', writes Beveridge, 'has consequences of a different order of harmfulness from those associated with difficulty in buying labour. A person who has difficulty in buying the labour he wants suffers inconvenience or loss of profits. A person who cannot sell his labour is in effect told he is no use. Jobs, not men, should wait.' Compare Say, 150 years earlier: 'The distress of a capitalist, when his funds are unprofitably engaged or in a state of inactivity, is nothing to that of an industrious population deprived of the means of subsistence. Machinery cannot die of hunger.'

There were three less known authors who gave the

first place in the problem of employment and welfare to the failure of effective demand, and particularly to the result of saving. They were Chalmers, R. S. Moffat, and Hobson. The last of these has been brought into notice by Keynes; but they form a chain in the same argument, since their dates of publication are 1832, 1878, and 1889.

Chalmers distinguished between capitalistic accumulation and consumers' accumulation. 'It is true of every single capitalist that he is all the richer by saving than by spending. But it is not true that capitalists collectively will become richer by saving than by spending.' This is because the rate of profit is reduced by over-investment. But consumers' accumulation by not spending accentuates the losses of capitalists, and reduces buying power; this is the loss of effective demand. Spending and trading must be in due relation to each other, or there will be general glut and depression. Those who say that this cannot happen are called the 'new economists'.¹

Moffat's argument was that consumption had not been given its due place, and that the distribution and habits of consumption were as important as the volume of production was to Smith. It was a fallacy to generalize saving as a way of increasing wealth; one person may profitably save, but not all. 'A general increase of parsimony would evidently diminish the demand for commodities, lessen the need for production, and reduce the amount of capital which could be held in organic relation to industry. The hoarding of the community is limited; the hoarding of the individual is practically not limited.' Real accumulation is not made by saving out of consumption, but only by industry itself, when the

¹ *Political Economy*, 1832.

final buyer replaces the capital through the price. 'Effective demand is the demand rendered effective by industry itself.' Abstinence itself gives no reward; the critical word is investment. In order that the profit motive may not gorge markets by over-investment, the buying power of labour must be maintained, in relation to its producing power, by a policy of 'labour-time'.¹

Hobson repeated the proposition of the other two that separate persons might save too much, while a community, or a Crusoe, would regulate saving. Every increase in saving and capital, in order to be effective, requires a corresponding increase in immediately future consumption. An increase in production does not force an increase in consumption because people wish to save as well as to consume. 'The desire to save may lead them to increase their production *independently* beyond the desire for present or immediately future consumption.' There is enough income to buy all the product, and replace the capital, if all the final product is consumed soon. But 'depression and excessive thrift describe phases of the same phenomenon'. Insufficient demand falls especially, by backward incidence, on the requisite of production which is, in any country, the 'limiting requisite', in least elastic supply. In Britain that requisite is labour, since capital can adjust itself, and the use of land depends on import. So that 'the East End problem, with its concomitants of vice and misery, is traced to its economic cause, and this economic cause is the most respectable and highly extolled virtue of thrift'.²

These three writers were the main stem of the

¹ *The Economy of Consumption*, 1878.

² *Physiology of Industry*, 1889.

argument on effective demand in relation to saving,¹ which was integrated into a system by Keynes. The system is new, the ideas go far back. For a long time, it was population which seemed to be the chief question, so that only recently has the appeal been made from the Malthus of the *Essay* to the Malthus of the *Principles*.

The germ of the modern analysis is therefore far older than the work of Hobson, to whom Keynes specially refers it. Both Smith and Mill regarded investment as the root of the question of unemployment; the employer who used a 'stock' in employing labour was their central idea. Demand maintained, but investment created employment. Mill's fallacy, that demand for commodities was not demand for labour, was a special case of this priority of the investment function.

Many reflections have been made on the 'classical assumption' of full employment. In the most recent statements of this view, no quotation or reference is given in support of it; it has become a conventional remark, which gives to the modern analysis the advantage of another supposed contrast with the past. But, indeed, a modern view is strengthened when it is shown to be a fuller perception of ideas which were growing into their maturity, rather than when it requires to

¹ Attention has recently been called to the work of David Laurie whose *New System of Finance* was published in Glasgow in 1815. Few copies of this single-chapter volume of over 1,200 pages are known. It is not in the British Museum, nor till recently the Bodleian, having been printed but not published. The author's problem is the tendency to industrial depression through the failure of purchasing power to keep step with the power of production. But his remedy is an increase in the elasticity of the supply of money. (See *David Laurie: Ein Verschollener Klassiker* in the Swiss *Zeitschrift*, 1945, by Professor E. Böhler.)

depend on the dangerous appeal to a new revelation. For example, the statement that 'the point of departure (of the new analysis) is that the level of employment can be effectively raised by changes in taxation, in the spending power of the government, or by other means',¹ should not be contrasted with, but related to, Mill's proposition that 'governments can create additional industry by laying on taxes and employing the amount productively', and that 'public loans are justified if otherwise capital would not have been saved or would have been used wastefully'. But there is a longer history than that of the antecedents out of which, however unconsciously, the doctrine of full employment has grown. Much of what has already been said about earlier perceptions of effectual demand is relevant here also, but some more special references have to be made.

More justice should be done to Steuart. He was the first to regard the provision of full employment as a duty of the State. While Smith gave only subsistence and public revenue as the right objects of political economy,² as the 'science of a statesman', Steuart had held that the object of an economy was 'to provide for the nourishment, the other wants, and the employment of every individual'. 'That number of inhabitants is best which is compatible with the full employment of every one of them.' 'Of what consequence is it to know how many people are in a country when the employment of them does not enter into the inquiry?' A 'free and perfect society' implies full employment for 'reciprocal and proportioned services between all who compose it. Whenever therefore anyone is found upon whom nobody depends, and who depends upon every one, as is the

¹ *Economics of Full Employment* (Oxford, 1944), p. 59.

² Bk. 4, Introduction.

case with him who is willing to work for his bread, but who can find no employment, that is a breach of the (social) contract and an abuse'. Then what is to be done? He is, among economic writers, one of the first planners in this field. He does not suppose that full employment can be got without policy; and he attaches responsibility to 'the statesman'. There is a 'vibration of work and demand'; either may fail to support the other. The case may arise when 'work augments, and no more demand can be procured; it may then be expedient to diminish hands, by making soldiers of them, by employing them on public works' or by emigration. 'Whenever the competition stands too long upon either side, the statesman must endeavour to load the lighter scale.' That is to say, he must act either on demand for goods, or on provision of work. 'From this principle flows the authority vested in all governments to load the country with taxes in order to advance the prosperity of the State, and this object can be nowise better obtained than by applying the amount of them to the keeping of an even balance between work and demand', that is by the 'imposition of taxes and the right employment of them to retard or promote the consumption of every branch of industry'. 'Under a frugal reign, numbers will diminish if the statesman does not open every channel which may carry off the superfluous products of industry. Here is the reason; a diminution of expense at home is a diminution of employment.' Steuart thought that, for the sake of full employment, the government should operate mainly on the terms of foreign trade, in the conditions of this country; a conclusion also reached more recently.¹

It goes without saying that Malthus is not among the

¹ Beveridge: *Full Employment*, p. 34.

classicists who can be charged with an assumption of full employment, and the long final chapter of his *Principles* is appealed to by Keynes. There is nothing on the subject, between Steuart and Mill, which bears on this question. There is a good deal of reference to the fact of unemployment in Smith, Senior, Lloyd, and Merrivale, but the observations are casual. At that time, it was population, not employment, which was the prior concern. There is no argument, in this period, of a relation of wage-rates to full employment. So we come to Mill, who became the economic teacher of the years before Marshall.

We have seen that it is often a quotation from Mill which is called 'Say's law'. In the *Principles*, Mill states a general proposition, that the means of payment for commodities is other commodities, and that 'all sellers are inevitably and *ex vi termini* buyers'. If production were doubled 'everybody would be *able* to buy twice as much because everyone would have twice as much to offer in exchange'.¹ He applies his limitation of this general case to the question of full employment in another place where he makes it plain that the general rule can fail, and for a reason in the nature of the case, the division of labour. 'Periods of brisk demand are also the periods of greatest production; the national capital is never called into full employment but at these periods.' 'The annual produce of a country is never anything approaching in magnitude to what it might be if all the capital were in full employment. This perpetual non-employment of a large proportion of Capital is the price we pay for the division of labour.'²

There is another line of thought in Mill, when he says

¹ *Principles*, 3, 14, 2.

² *Unsettled Questions*, Ch. 2.

that 'it would be possible for the State to guarantee employment at ample wages to all who are born', but only if it could control the birth-rate.¹ Otherwise, the individual product may, by force of numbers, fall below the necessary subsistence wage, and there will be unemployment. Here again full employment fails for an essential reason, the laws of population and diminishing returns. It should also be noted that, even if population can be controlled, the possibility of full employment is made to depend on an action of the State which, as we have seen, can create 'additional industry' by laying on taxes and employing the amount productively.²

It is therefore impossible to ascribe to Mill the opinion that full employment was a result of the free operation of the economic system. It is not unusual, in any analysis, to indicate the limiting case, where conditions are ideal, and to proceed to allow for the actual qualification. The ideal must also be allowed for in the modern analysis; because there, full employment will result from the Minister's policy only if his proposals work ideally, that is to say, if all the estimates of investment are correct, and all the statistics faultless, and there are no disturbances or interferences. If, for instance, an average of 3 per cent of unemployment must be allowed for, as Beveridge argues it must, the necessary minimum of 3 per cent will often be exceeded.

The modern analysis gains rather than loses authority by recognising, instead of depreciating, the growth of its ideas in the work of earlier writers. In the same way, the modern is more strongly placed if it expects to be absorbed in, rather than discarded by, the more modern of the future.

¹ *Principles*, 2, 12, 2.

² *Principles*, 1, 5, 2.

CHAPTER 5

DEMOCRATIC SOCIALISM

There are stages in the growth of public agency, from necessary legislation up to total socialism. The phase called democratic socialism is a compromise, in which the doctrine of socialism is qualified by reference to some special conditions. These sanctions of a limited socialism are the fundamental nature of some industries, the fear of private monopoly, the consent of the operatives, and the prestige of public ownership. The strength of these sanctions is thought to justify an experiment in efficiency.

THE economic doctrine that full expenditure on consumption or investment will maintain full employment goes in favour of keeping the system of private enterprise, though it will work under the influence of a public policy. There will be official action to compensate a foreseen gap in total expenditure, but this will be of the nature of public outlay, or of measures to influence private outlay, not of public management of a sector of industry. It is not desired that the public activity should be on a large scale; it is rather preferred that it should not be necessary. It is expected that private enterprise will continue to be the main form of the actual management of industry. This adventure, as it has been called, in economic policy is supported by a theory which is now held with great confidence; we have to go back to free trade or the gold standard for recent examples of equal confidence in the finality of a theory of policy with similar deprecation of the alternative.

We have seen that this theory of policy has been nascent in economic literature over a long time, and has

been one of a number of competitors in the solution of the problem of employment and distress. The theory and policy of public economy, as Gladstone understood it, gave way before the war of 1914 to a spending policy on social purposes which doubled in fifteen years a budget which had formerly taken fifty years to double itself. Protection won its battle with free trade in 1932. The other competitor was the control of population, on which policy has been reversed. In a sense, effective demand could be said to be an aspect of what was claimed for the other theories, and to have finally emerged as a policy in its own right.

Also, we have seen that professional economic thought did not support a policy of public inaction or make any assumption of full employment. Free traders and protectionists each thought their policy to be preferable to the alternative, and economists were free traders. A theory of better employment did not assume full employment.

Full employment has emerged from the conflict of particular policies by separating the concept of effective demand from its special connections. Effective demand has had a continuous history in English economic thought since Steuart. It was not well handled by Malthus, but he had a strong sense of its importance. It did not develop straight from Malthus, but it was one among other considerations in the rival trade policies of the nineteenth century. What Keynes did in 1936 was to make it a leading, and not merely an involved idea.

The success of Protection, and the rapid growth of the social services have affected the attitude toward State agency. There has been a natural development of three spending policies, the one-time of the Lloyd-George pamphleteers, the intermittent of the Webb school, and

the programme of continuous readiness of the Beveridge plan, based on the theory of income which is now under trial.

It was not a part of this policy that there should be any public industries. But political events have moved faster than economic theory, and have created a new condition. There is being created a sector of public industry, of a limited area, which may seem to increase the directness of the public policy of maintaining employment. The initial limitation of the sector to a suggested one-fifth of industry shows that liberal opinion has made some impression on Socialist doctrine. At the same time, this amount of nationalization seems to keep something in reserve in case the spending policy does not have the expected effects on private enterprise or investment. The theory of full employment has been expressly separated from the policy of nationalization, as it was from implication with other special policies, but it will now work in the conditions of what is called 'democratic Socialism'. This policy is subject to choice by political election; it gives the State a sphere of direct industrial control; and it leaves a wide field for private enterprise. All these conditions may be regarded as aspects of industrial policy in a country influenced by the ideas of political democracy.

The socialization of an industry is usually defined by the motive of production for use instead of for profit. The industry has, however, to be profitable, in the sense that it must be able to pay for labour and capital at normal or standard rates. An industry can make either of these rates abnormally high by limiting its output and increasing its unit selling price. But it is managed socially if it aims at the largest output and the lowest price which enable it to find employment for labour and

capital at the rates which at the time are normal; that is, which enable it to retain its supply of labour and capital. This means the maximum public use of the product, and the maximum of employment. If the public demand for the product creates a surplus over the normal expenses on labour and capital, that surplus is to be applied either to the further development of the industry, or to some public purpose, or to reserve funds against fluctuations of the demand. It is a possible result of theoretical analysis that the public might gain if a particular industry were run on a financial deficit, paid for out of taxation; but practicable socialism does not go beyond the proposal that, over a period of years, the industry shall pay its way, and shall manage its finances accordingly. This does not prevent a socialized industry from adjusting its prices in special markets to the needs of special consumers, in order to develop these markets, or as concessions to special needs, or to restrict undue expansions, subject to the general requirement that the industry as a whole is not parasitic on the taxpayer, and therefore on other industries.

The phrase 'democratic socialism' has now come into use to define the British development. This does not mean that a socialized industry is to be managed on the principles of political democracy, whereby every member of the industry would vote for its leaders, who would then act as representatives of the employees of all grades. 'I think', said the Socialist President of the Board of Trade, while the Coal Bill was in Parliament, 'it would be almost impossible to have worker-controlled industry in Britain, even if it were, on the whole, desirable.' It is doubtful whether the political model of government is applicable to any other sphere than politics. It does not obtain in the military, or in large parts of

the ecclesiastical, sphere. Trade Unionism is not industrial democracy, it is collective bargaining, a quite different idea. The government of a socialized industry is chosen on qualifications, and it then acts by authority.

Democratic socialism means that degree of socialized industry which a modern democracy is thought to require, and depends on showing that the whole national economy needs to have a sphere of public control, either because of the conditions of some industries, or in order to prevent an undesirable degree of private authority. These conditions will be discussed later. Democratic socialism is therefore a limited socialism. It seeks an equilibrium between the spheres of public and private enterprise and, as this is a matter of argument and proof, it differs from that general theoretical imposition of socialism which is called communism. This openness of argument on what should be socialized is an aspect of the democratic choice. Of course, this is subject to political methods of election being themselves really democratic; a majority of constituencies may be far from representing a majority of electors. This disparity is important when great changes of policy are in question. Democratic choice can bear only its usual interpretation. Of course, also, that choice is subject to revision or extension of its first proposals. If only, so to speak, a Sudetenland of private industry is to be immediately occupied, with 'no further territorial ambitions', it will be remembered how the 'logic of events' amended this proposition in another case.

In view of the long critique of private enterprise which socialists have maintained, it seems at first paradoxical to conclude that democratic socialism should still leave the greatest part of industry under that system. No doubt, there is a difference between allowing

private enterprise to range as it finds profitable, and giving it a limited and considered range. But this would be too strong a reflection on the new programme; because the unsocialized part of the economy is to have gradations of control, which belong to the sphere of policy rather than of plan, under new laws for Councils of Development for particular industries, as well as under the general review of a national policy of investment. Of course, such measures are additional to such ordinary legislation as takes place already by the Company Acts. So that democratic socialism intends to have a penumbra round the sun, not the black outer darkness ascribed to free capitalism, and the two kinds of organization are to be geared to each other by a general concept of the public interest. In that case, the two spheres of industry, public and private, may end a long controversy by coming to a friendly settlement. It is not yet certain whether a real compromise of social thought has been reached. Socialist policy has behind it a strong historical momentum, and a critique of private capitalism which it is not easy to revise. On the other hand, the examples of 'total' policy in other countries is creating a sense of restraint. The question is whether an equilibrium between public and private enterprise is stable, when it is not based on what are clearly the necessary functions of government. The sanctions which we shall proceed to discuss, as ostensible reasons for public administration in a certain sphere, do conceal something near a crisis in economic thought.

We may here recall the distinction between policy and plan. A policy is directive; a plan is executive. A policy uses an instrument, and depends on the consequences of that instrument; it does not go further. It

supposes that the instrument will lead people to act in the way that is desired. Family allowances are the instrument of a population policy; the instrument being given, the actions of persons are relied on to obtain the result. Bank rate is also the historic instrument of a policy of directing investment. The scheme of full employment depends mainly on instruments of policy for inducing the free reaction of individuals according to their interests. When the government says that the largest part of our economy is to be private, this means that it is subject to the method of policy. But a plan is executive; it sees the thing done, and does not only rely on other persons to do it. Then you have to nationalize, and command your officials. The natural assumption is, that policy alone is not thought to be strong enough or certain enough to obtain the results you want.

So there are three aspects of the question of public agency. There is necessary legislation; and the scope of this must increase with the development of society. There could not be Factory Acts until factories had superseded domestic industry; but there had to be Factory Acts then. There could not be Company Laws until there were Joint Stock Companies; nor Combination Laws till there were Trade Unions. Necessary legislation was at one time thought to be limited to protection against force and fraud; but at that time the nation had not developed the activities which must have extended the meaning of necessary legislation. It is therefore absurd to ascribe the earlier idea to modern policies. Second, there is directive policy, which came into the question of public agency, because it was inseparably connected with the way in which the national finances were arranged. The chief directive instruments have been forms of taxation, or relief of

taxation, or financial assistance, acting upon personal motives. Third, public administration; and this could not come into the question until a later stage than policy, because industries or services had to grow into large units of private administration before they could be considered sufficiently unified for transfer to public hands. This is called the planning stage. It had to come late, so that earlier objections to nationalization may have been valid at their own time. The sphere of public agency is almost necessarily a function of national development.

Nevertheless, the step from directive policy to public administration is contested in our time of high industrial organization. The crux of this contest of opinion is industries rather than services. As far back as we go in economic thought, we find the right of the State to organize services admitted or not barred, at a time when Socialism, as we understand it, was as bitterly opposed as Communism is now. When writers like Malthus, Senior, Cairnes, McCulloch and Mill argued that *laissez-faire* was no matter of principle, but only one of evidence, with the burden of proof on any new public function, they were not thinking so much of public industries as of the extension of services. It is in the last hundred years that the onus of argument has gradually shifted to the nationalization of industries, which has been strongly opposed by, for instance, the Liberal party's programme of organized public services of health, insurance, and security. Liberal thought has continued to see a difference between what may be called social socialism and industrial socialism. Despite the great organization since Lloyd George of social socialism, it was felt that a Rubicon was crossed when the coal industry was nationalized.

Another way of reconciling the authoritative aspect of Socialism with democratic ideas appears in recent proposals to nationalise only some parts of an industry, or to establish public factories in competition with private ones. It revives, in the form of a fundamental freedom, Smith's statement of the private right to apply one's labour and capital. If it is developed as a political compromise, it recalls from oblivion Mill's concession that "there might be a national bank or a government manufactory, without any monopoly against private banks or manufactories," and the same as regards schools and hospitals.¹

The question now is, what are the grounds or sanctions on which this new function of government is recommended? And we are asking this question on the assumption of a democratic environment, such as we have in this country. Where that does not exist, the question is short-circuited by the assumption of totalitarian government. In a democratic country, the change from private to public industrial administration is a matter of choice, for reasons which commend themselves to Parliament.

The inter-war Committee on Industry and Trade (Balfour Committee) said that they did not 'conceive that the usual antithesis between public and private enterprise is based on any fundamental economic principle which is valid in all circumstances and at all times. On the contrary, it is evident that there is a proper place and function for both these forms of management, and that the question of their relative advantages in any particular case is a practical business question, to be settled on the same principles and by the

¹ *Principles*, 5, 11, 1 and 8.

same criteria as are applied to other questions of industrial structure'.¹ While this was a remarkable admission in 1928 from a Committee of mainly business men, it is not a quite correct statement of the question of nationalization. Public monopolism is a change of government far more than a change of structure; and the change in the Coal Trade was not what the Committee calls a practical *business* question. Municipal monopolies of local services like transport or gas do not mainly alter the structure of these services; the reasons for the change have been quite different. In respect of nationalization, the reasons lie in questions of ownership, even if there is a change of structure, and why is the difference of ownership thought to be right?

The arguments show that the following four considerations are now the real sanctions. First, the fundamental nature of certain industries; second, the problem of private monopoly; third, the consent of the operatives to the existing private system; fourth, the simple prestige of public ownership. This list means that simple business efficiency is not one of these sanctions. But it is right not to consider this as one of the claims; the claim really is that public ownership can be as enterprising as private control, and that it can at the most maintain efficiency while overriding certain objections which arise under even the most efficient private management. This is particularly clear by the fact that the proposal to nationalize the steel industry was made at a time when its high efficiency was admitted.

First, as to fundamentalism. It is not a simple, but a complex idea. It includes three senses in which some industries or services are particularly *important*. These are the senses of what is general, what is dominant, and

¹ *Industrial Efficiency*, II, p. 42, 1928.

what is essential. There are some services which are rendered generally to all industry, the chief of which are transport and banking. Then there are some industries which are dominant, because their products enter largely into the processes of other industries, whose activity therefore is always in a state of dependence on the availability of these products. Coal and iron are the chief cases. And there are some industries which are essential, without being dominant, because their products are a condition, without entering into the process, of activity elsewhere. Agricultural food supply is the chief instance. The same economic argument does not apply, under the same word, for these different senses of what is fundamental. Agriculture is not fundamental in the sense in which coal or iron is; nothing else is fundamental in the sense in which food supply is. The importance of fundamental industries or services could be translated into a common idea of the *dependence* of the economy upon them. This dependence in turn has created the objection to the private control of what we most depend on. When other industries are said to be 'ripe' for nationalization, what is meant is that their organization has reached a stage of 'high capitalism' such as both to suggest and render practicable their transfer to a single authority. Many industries may ripen in this way, without the objection to continued private control which is felt in the case of the fundamentals. There is involved a social question of authority, as well as an economic question. This may be enhanced by the complexity and secrecy of the arrangements within highly capitalized industries. The fact that agriculture is not in the first list of industries to be nationalized, in spite of its size and essential supply, is due to its not being highly capitalized; it does not create scope for

magnates, and the national dependence on it is impersonal.

Dominant industries, whose products permeate the economy, have great powers of control through the prices of these products, which are other producers' requisites. Even if these powers are not objectionably used, the government may think that they can be used to advantage in public hands. Thus, the first Section of the Coal Act makes it a duty of the Coal Board to use the price of coal in whatever way 'may seem best calculated to further the public interest in all respects'. It had been an argument of the foreign Coal Cartel that they could in this way control the trade cycle through adjustments of the price of coal as a requisite of industrial expansion. In this country, the control of the price of credit through Bank Rate was the chief form of this idea, since credit is also a requisite of expansion. Bank Rate did not act in this way, as a cost, but because a reduction of that rate increased capital values, and therefore raised the price of constructional materials so as to nullify its own influence as a cost to merchants. But the prices of the products of dominant industries act on expansion elsewhere as direct costs, the use of which, by methods of discrimination, are thought to be less objectionable in public than in private hands. So that the nationalization of these fundamentals may be simply an aspect of planning. The Bank was nationalized because its control was already in accordance with public policy, and dominant industries in case it was not.

Second, the avoidance of private monopoly. It must be agreed that in a democracy this is an important sanction. A monopolist control affects not only the consumer by high prices, but also the worker, through

restriction of output and work. The same results are now held to exist, though in less degree, under monopolistic competition, which finds its equilibrium by running short of capacity at a price above minimum average cost. That is, if there is an equilibrium; but experience shows, as Marshall had argued, that the competition between a few highly monopolistic producers disorders the market altogether. The traditional industrial safeguard against private monopoly has been the freedom of new producers to come in against it; but only large scale new producers can effectively come in against a monopolist, so that the market is either over-supplied with capital, or we have either the restriction of running short, or the outbreak of excessive and demoralized competition, with the use of many forms of what are called trade practices; boycotts, rebates, preferences, price discriminations, and so forth. These bring in the question of what is fair trading; and the State has a concern for that. So that price, employment, and fair trading, affecting the consumer, the worker, and the producer respectively, are involved in monopolistic policy and control. Even if there are great potential economies in monopoly, they cannot be relied on to emerge and be handed on. If these economies are very great, it has been argued that, even if they are not fully handed on to the community, as much as is handed on may enable better prices than smaller producers can give. But this argument generally rests on the fallacy of comparing the monopolist with the small producer; in fact, the condition precedent to monopoly is a few large producers, who have already reached the stage of great potential economies of supply. There is no theoretic argument which out-flanks the danger of private monopoly. When you have this danger in fundamental industries, two sanctions for

public action coincide. But among the earliest trusts which had to be controlled were those in sugar, tobacco, and spirits, so that the range of the question is wider than fundamentalism.

It is no longer possible to rely on foreign competition to control domestic monopoly. There were, in 1939, more than 150 international economic agreements between national combinations of producers, and these included copper, aluminium, rubber, steel, oil, tin, lead, wheat, nitrates, potash, phosphates, sugar, tea, rayon, cellulose, electric lamps, cables, porcelain, enamel, and many other staples. By such agreements, nationally associated producers divided the world's market between them and, in many cases, reserved the home markets to themselves; that is to say, superseded any import duties by complete prohibition of import. This was the most dangerous development of private monopolism; it is true that governments were themselves parties to several such agreements, while they connived at many more, but that was public policy, while the private international cartels were not.

Now, granting the seriousness of this economic development, it may still be argued whether it forms a sanction for public monopoly. In both America and Germany, where the problem was most similar to ours, statute law was devised to prevent the abuse of economic power, and the United States still regards this as the right procedure. In this country, we had no statute law against monopoly until 1948, and the Act then passed follows in its general outline the American legislation which began in the Sherman Act of 1890, and was made more detailed since 1914. Until 1948, we relied on the Common Law, but this was used in a narrow legal manner, which disclaimed any argument of an economic

kind, and which has on the whole been favourable to monopolies. It is better to have a warning law, like the Sherman Act, than to twist outdated legal precedents to modern conditions of industry. It could be held that industrial law ought to be the first resource in this matter, and that it should not fail in England to be as effective as the Federal Trade Commission has been in America, or the Cartel Decrees were in Germany. At a time when it was introducing the first statutory legislation for control over monopoly, the Government could hardly at the same time argue that it must suppose the proposed legislation to be inadequate for its purpose. In the cases of Coal, Transport, Banking, and Steel, in which the government was committed to nationalization before its Monopoly Act was passed, it must be assumed that other sanctions than monopolism were mainly in view.

And this brings us to the third sanction, which I call the consent of the industry. Is the industry being worked on a system to which the parties consent? Or is there some fundamental dissent which prevents the industry from working at its proper capacity as a public service? This problem of consent appears to be one of an industrial psychology which does not obtain in all cases, but which has been specially marked in some cases. It has for a whole generation affected the miners, and to a less extent the iron and steel operatives. Does the special psychology of these men, and particularly the miners, arise in some way out of the conditions of their work? Or do the conditions of their work make them specially receptive of Socialist argument, to which other operatives were not so sensitive in their own case? Or has the personality of Trade Union leadership been more forceful in their cases? It seems that all these have contributed

to this problem of consent. Here we may refer to some admissions which have been made authoritatively. In 1946, the President of the Trade Union Congress pointed out that, in the past, Trade Unions have had to impose restrictive measures to protect the workers' interests and to lessen the evil of unemployment. 'But I suggest', he went on, 'that in the new situation resulting from socialising legislation, the unions will have to reconsider their attitude towards many of these restrictive methods and practices', for the reason that 'these stand in a different light when it is the public interest that is served by every managerial and industrial development'. Now neither the President, nor other political leaders who made a similar statement, specified the restrictive powers to which they referred; but one can hardly imagine any which are not restrictive of output and employment. And it would not be fair to press this so far as to make it imply that the strike should cease to be used in nationalized industries. Indeed, it has already been made plain that it would be difficult to guarantee this. But the admission of restrictive practices means that there has not in these industries been an unhampered test of the efficiency of private enterprise, because of the industrial psychology of the operatives. In other words, in comparing the pure efficiencies of public and private enterprise in these cases, there is a certain amount of slack to take up, so that public enterprise, even if technically less efficient than unhampered private enterprise, might offset that by some greater degree of harmony between management and operatives. It may not be a reason of the first order for the nationalization of industry, particularly if a full employment policy is being sought by other means. The whole programme of social security appears to lessen the significance of those

arguments which seek the defence of labour conditions in a change of industrial management. We must conclude that nationalization for the sake of consent to the system has a sanction simply in the historical momentum of the psychology of some important industries. Of course, we have seen the contrary application of this sanction in the case of the doctors.

The last sanction to consider is a somewhat vague one, but it appeals to many people. It is the prestige or dignity of public ownership. Many people, and types of people, derive satisfaction from the feeling that our mines and railways are now our own mines and railways; and such people have this feeling as citizens, not as the operatives of these industries. To such people it is worth while to see 'British Railways' painted on the engines, or the flag of the N.C.B. over a pithead. To put it conversely, they perceive an indignity in private ownership, especially in respect of great or fundamental industries, which has been described as making the artisan an 'economic lodger' in his own country. This is not the same question as the profit motive. It is just an outlook of citizenship. It appears to go a good way in Russia in creating a public spirit which surmounts many restrictions which would otherwise be discouraging. In this country, it is especially observable in respect of the municipalized service industries.

It may still be asked whether we have not left out the most important sanction of all, that of efficiency. So it should be realised that the question between public and private efficiency in the control of a certain group of industries is not a settled question. Some economists, like Marshall, held that the probabilities were heavily weighted against public management on this score;

but others, have given reasons for being less dogmatic. John Mill thought that the increasing scope for delegation of management met many objections to Ministerial control of industry; and based his objection finally, not on technique, but on interest. 'All the facilities which a government enjoys of access to information, all the means which it possesses of remunerating, and therefore of commanding, the best available talent in the market—are not an equivalent for the one great disadvantage of an inferior interest in the result.' But it is not certain that this is now the difference. Interest in the result has now a wider meaning than Mill considered. A further stage in the organization of industry takes with it a further stage in the methods of social expression; they are both phases of the course of administrative change. The Coal Act of 1946 sets out the first framework of nationalized industry in this country, so as to allow a number of interests to be expressed. There was a related change of industrial and social forms of action. The Coal Act required the Board to include persons who had experience and capacity in 'industrial, commercial, and financial matters, applied science, and administration', so as to bring expert judgement from outside the coal industry to bear upon that industry. Second, consumers' Councils were set up, who could refer to the Minister any defects they observed in the administration. Third, the industry was to be managed so as to pay its way, including rates and taxes, over an average of years, on strict accounting principles. And fourthly, there was a final reference to criticism in Parliament of its proceedings and results. These forms of criticism are the substitute for industrial competition in this case, where foreign importation is not an active force. They reduce to a specific issue what had long

been argued in general terms about the relative interest on which public or private industry could depend. No special qualifications were required of the Minister himself, or could be applied, in spite of his powers to direct the Board; but he represents a permanent staff, by which he is advised.

It is open to say that these grounds for a policy of nationalization are really subsidiary to a point of view which short-circuits detailed argument; that is, to the purely Socialist doctrine of the class conflict. Or to a modification of this doctrine by the idea of economic trend, which gives public ownership as the final extrapolation of production on a large scale, or industrial socialism as the extrapolation of what we have called social socialism. As the holding of Socialist opinions is no longer a question of class, special argument is required where this feeling does not sway opinion; and the theory of trend, or 'inevitability' of evolution, is not enough. Hence the sanctions which we have considered.

These different lines of thought on nationalization are marginally controlled by each other, within a limit which depends on how much a government with urgent political duties can efficiently undertake. In war, the government accepts industrial and political functions at the same time, for the purposes of a short period. In peace, the sphere of government does not depend on such urgency and can be more freely chosen. The adjustment in a political democracy depends on such conditions as these. On there being a field of private enterprise large enough to maintain inventiveness, both for private industry itself, and for contribution to public services of invention and skilled personnel. On the fact that nationalization, while technically reversible, is not on political grounds easily undone, while the

measure of its efficiency is capable of much political disguise. On the fact, finally, that nationalized industries have to be administered by changing governments, some of which believe in that system while others do not, so that it should not be carried further than its political acceptance can be considered to be fair and democratic.

CHAPTER 6

ECONOMIC ASPECTS OF WAR

In a sense, war has 'faulted' the trend of economic progress. 'Post-war' and 'pre-war' tend to have biassed meanings. War is incidental, rather than evolutionary or accidental. War policy finally goes back to the land. The net contribution of war to economic progress has depended on forced experiments in organization, and liberal endowment of special kinds of research. The strength of effectual demand during war does not prove the same possibility in peace.

THE wars of this century have been on a scale which has caused new views to be taken on the relation of war to progress. Up to the middle of last century there were lingering reminders of the French war in Parliamentary debate, but the legislation of 1846 was not proposed or opposed on the ground of its effect on national security. After that, our finance began to have some reference to war-time reserves, but it was easy-going, a matter rather of the cost of peace than of the probability of a great war. The outbreak of another such war was a sort of limiting condition of social or economic thought, and our economy was allowed to proceed on assumptions which involved our national dependence on supplies in conditions of peace. The recurrence of the Protectionist debate was concerned with such questions as Imperial unity, dumping, employment, and aspects of prosperity at home.

The wars of this century have created an economics of the subject. They have not come and gone as outbreaks of disorder from which the economic system had only

to recover and resume its trend. They have influenced thought and policy both by reflection on the past and adjustment to the future. Pre-war and post-war are not merely historical terms, they are used to imply that the trend of both events and thought has 'faulted', and displaced the seam, and made a new level of ideas and events. 'Pre-war' ideas and policies are given this label with a suggestion that war has done something to clear our minds, and to show defects in our ordinary arrangements, which defects are seen from the new level of 'post-war' thought. The first war revised our views on monopolistic combinations, the second made bye-words of free trade and the gold standard, though they had been gospel for seventy years. These became 'pre-war' ideas, not because they were out of date in a war-endangered world, but because of an alleged enlightenment through the flash of war. The second war made this attitude somewhat difficult to adhere to because what had been post-war became pre-war. But the inter-war period came to be regarded as not post-war enough, because of some tendencies toward recovery of pre-war policies which the second war is thought to have effectively antiquated. For at least a large part of that period, economic thought, and the conclusions of official and other inquiries, rather fancied a qualified adherence to the gold standard, free trade, and private production of staple commodities, but the equilibrium was too unstable against another war.

The faulting of the trend by war is the result of several influences. There is the experience of war-time organization; the pace of war-time technical inventiveness; the burden of war-time finance; and what may be called the war-time shift in industry, location, and methods of administration, on which it is easier to go forward than

back. It is this shift which, if a war is long enough, vests its results into a vested opinion which makes it difficult to have a free reconsideration of post-war in relation to pre-war conditions.

The human cost of war is so great that compensation for this may be sought in a comparison of the pre-war and the post-war on stronger grounds than mere economic enlightenment. After both the wars of this century, but especially after the second one, it has been sought by some writers to give war a necessary and beneficial function in social evolution. 'Wars of this (total) kind break up and sweep away the half-rotted structure of an old social and political order, and lay the foundations of a new.' 'War is at the present time the most purposeful of our social institutions . . . the most powerful known instrument of social solidarity.' 'The one thing war never does is to maintain or restore the *status quo ante bellum*.'¹ Now, in the first place, it is out of the question to make so sweeping a statement on the basis of two wars only, which were connected with each other; one would suppose, from such statements, that wars of important size were a regular feature of history, like trade cycles, regular enough to make an inductive conclusion possible in a general way, and this is not the case. War is not an institution. We had no experience of war between 1815 and 1914, on a scale which would give any meaning to such a phrase as 'what war never does'. Other wars may yet be fought in defence of our social institutions, and lead us to confirm them. It was a common charge that the war of 1914 did not do anything so drastic as 'sweep away' the pre-war economy. We are not in a position to make propositions of the kind quoted above. A successful belligerent must be in a very different case

¹ E. T. Carr: *Conditions of Peace*, ch. 1.

from an unsuccessful one, and may fairly attribute some degree of its success to the merits of its pre-war economic system. Russia does not intend, as a result of the second war, to reverse her communist system, or regard it as 'half-rotten'; the war has confirmed her in it. Burke said long ago that 'war does not leave a nation where it found it', but this is not one of his most substantial contributions to thought.

In the second place, such general inferences neglect the cases in which great social and economical changes have happened without war. Neither parliamentary reform, nor free trade, nor the socialist movement came in because of wars. The social legislation of modern times had its foundations laid before the Great War. The free trade creed, regarded by its opponents as the greatest of nineteenth-century mistakes, survived the first war, and was reversed by something quite contrary to war in its nature, the Great Depression; the same is true of two other pre-war 'faiths', the gold standard, and public non-interference. It was not the second war which upset them, that had been done already. Of the ideas which have been extended and confirmed by the two wars, the combination movement in industry, the women's franchise, and the endowment of families, were all in the trend of events, war or no war.

Above all, the wars of this century have not swept away, as a half-rotten structure, militarism and military preparation. The experiment of war leaves this pre-war aspect of national life still in a condition of such strength that modifications of pre-war competitive capitalism may not be of relatively greater importance for the future form of our economy.

If we have not the evidence by which to define war as revolutionary, can we regard it as either catastrophic or

evolutionary? It is not catastrophic, because it is by the deliberate act of some nation that war is made; people do not make earthquakes or floods. Neither do they set out to cause great depressions of trade, like those of 1886 or 1931. These are catastrophes, although they are, like earthquakes, the outbreak of hidden forces. Whatever the impact on individuals, for a nation as a whole, a catastrophe is a result which nobody intends to bring about. Nor is war a result of economic or other tendencies so necessary that it can be called evolutionary in its nature; no one supposes that the great wars could not have been avoided. Between accident and evolution there is the intermediate phenomenon of what may be called incident; and great wars may be described as incidental. The impact of accident is from outside; it need not have happened. Incident is an event the conditions for which arise within an evolution, but which can be postponed or anticipated or averted by the influence of personalities, or by some coincidence or antagonism of other influences within the phase that evolution has reached. War is a precipitate of danger in evolution; and danger is a lasting condition of many human relationships, in which rights and claims evolve, so that classes and parties and nations may for long periods be living dangerously. Danger is a condition which re-requires continuous attention; it is itself quite evolutionary and normal. Whether it does or does not result in breakdown, by strikes or crises or wars, is not indifferently or equally normal. Clausewitz held that war and diplomacy were two aspects of one activity, that of imposing your will on another party; even so, they are the alternatives of normal and abnormal. In his classical book on war, the abnormality is completely obscured by the absence of any consideration of what it

is that has to be done, or what a bayonet is for. And a general theory of modern war requires an even more effective *alibi* from such considerations.

Classes and parties and interests ought not to use the calamity of war so as to create a pillory called 'pre-war', in which they place any aspects of national life of which they have been critical, labelled, by a naive use of the *post hoc* as the *propter hoc*, as the 'war causes'. There is, in a democracy, a continual criticism of all social institutions, and a continual legislation about them, and it is a great strain on belief to suppose that there were particular dates, 1914 or 1939, when a failure to proceed on these lines coincided with a crisis in international diplomacy. To the pillory of 'pre-war' there corresponds the gold-framed picture of 'post-war', of which the world had twenty years of experience after the first great war, and is now experiencing it again. Is it true that a 'rotten structure' of economic life had developed in the first 'pre-war' century of 1815 to 1914, and another one in only the twenty 'post-war' years 1918 to 1938? For, if so, great wars appear to accelerate the oncoming of social crises, rather than to sweep away their causes.

This argument should not be necessary to those to whom war has been an experience as well as a word, or economic history a study. The danger is that the purgative theory of war persists, and that the war spirit is deeply embedded in secular and religious literature. Also, it is a danger that the analogy of war is transferred to other forms of conflict—such as trade or tariff 'wars', or the propaganda of sects and cultures—so that in social thought there is a sort of margin of indifference at which such false analogies touch and tempt real war. This dilution of the idea of war tends to blunt the edge of moral criticism, till it is only sharp enough to cut the

butter of what is only 'human nature'. When the metaphor is extended to social purpose, and we make 'war' against unemployment, squalor, or poverty, it acts in reverse, so as to enhance the parent idea, and give it the sanction of the best motives. The famous Budget of 1909 was described as a 'War Budget' when its claim was placed highest. The concept of war is thus standardized, and seeps into common thought, even although all these metaphors are false, since real war suspends fundamental ideas of human conduct and relationships.

Both small and great wars have an economic aspect of their causation, in their relation to territorial power. It is this relation to territory which connects war with the general forces of supply and demand; although the occasions of war may disguise the relation. Whatever else is wanted by a nation which makes war, it is increased control over territory which makes its realization possible; by such means as self-sufficiency, outlet for population, access to materials, strategic advantage, or the interests of nationals or co-religionists anywhere. The result of war is usually some re-arrangement of territory. Successful war gives a nation increased power to make or influence the general arrangements of the world, in accordance with its own ideas or interests; the aspects of this fact are numerous, but they lead back to territorial jurisdiction or influence. Against this, rational argument has been applied with a view to showing that the ownership of territory is, for the purpose of material advantage, a 'great illusion'; but this argument has failed against the instinct that territorial influence is the basis of all other advantages. The world area has a limit, but its population has not, and the desires of the populations which exist within nations are not limited either. How, it has been asked in lines

continually voiced, ought its citizens to adore a land of hope and glory; the answer is a prayer that its bounds shall be set wider still and wider. It is not realized that this is demand and supply, in one of its various disguises. It is a phase of the growth of business interests, as they grow in the scale of their work, that they seek to ensure their supplies and independence by 'integrating' the sources of supply, and owning where they formerly bargained. On the national level, to bring previously external arrangements into your own hands, for national purposes, is a more varied expression of the same tendency to integrate. Nations make treaties, as business enters into combines and cartels; but beyond these is the special security of direct control over supplies and areas. It increases the power of a nation over the general arrangements of the world, a power which effects both its interests and its prestige. Territory is the fundamental aspect of this, almost by the definition of the conditions, so that, under whatever disguise, war always takes us back to the land. The ultimate problem of the United Nations Organization will be, whether the frontiers of nations can be finally stabilized.

It has been held that the private capitalism of the last century has been an influence tending toward war, because territorial influence extends the markets of a nation, or gives preferences to its producers. That the private production of armaments may have such an influence is a different and more special question, which can have a particular remedy. In what way can capitalism be related to war? The former is an industrial, the latter a political fact. The interests which are called industrial may be able to exert an influence on those which are called political; or the political interest may spontaneously act with regard for the industrial.

Capitalism is a feature of all modern manufacture, public or private. By itself, it supplies no argument about war, unless that war has some relation to industry which did not obtain in pre-capitalistic times. War is too old for that. It comes closer to the question to say that capitalism has taken a particular form, such that investors and operatives are not both shareholders, but are separate groups, related only by bargaining. Capitalism thus became the interest of the former group, which held the capital, and directed the policy. If, by some equation between a unit of money capital and a week's work, all employers and employees became shareholders and voters, this separation of interest would be bridged over. The profit motive and the wage motive would be included in the gain motive. The persons responsible for policy would be chosen by both sides. It is possible to argue that this would modify the pressure of industry on politics, for the sake of markets, which is regarded as a cause of war; but it could not be assumed. It could be said that, on the present system, the separate dividend interest creates a class who take a wider view of industrial interests, because investment can be spread over all kinds of industry, while labour is limited to one; and that, in this class, the growth in the scale of industry and investment creates a group of industrial politicians who can influence public international policy. There is a history of such magnates, to whom an interest in war is often ascribed. It is fairly difficult argument because of the international business structures in which such magnates associate. All such reasoning may appear forced in face of the more obviously political causes of most wars. The substitution of public for private capitalism may obviously increase 'nationalism', since public industries will not be international,

so that industrial might reinforce political nationalism. This is quite speculative. The United States is the most privately capitalistic of modern nations, and remained out of both the recent wars until it was forced to enter them. In the second war, the aggressor had a system of National Socialism already in existence, with which the kindred system of Communism made an alliance, and waged war on Finland. Then the two nations who were most critical of private capitalism made war on each other, with the cognate system of Fascism choosing one side. So that, for the making of war, the priorities of economic structure, and national purpose, are not easily distinguished. It is not possible to read the history of war without perception of the influence of personality, which makes war neither accidental nor evolutionary, but incidental.

The relation of war to economic progress has been argued in a number of ways. There is, during war, a degree of forced experiment in the organization of industry, and an increased tempo of certain forms of invention, and a great deal of destruction of property which creates a new and unsought condition for better forms of replacement. This account should not be added up without reference to the lapse of time during which changes in organization and invention and replacement would have been running their course under other than war influences. War causes events to be dated as pre-war or post-war, and it is necessary not to allow this terminology entirely to replace the difference between 'six years ago' and 'six years after'. Much of the social outlook of what is 'post-war', though not all of it, is due to the resumption of ideas which were suspended in war-time, and with which we might have been further forward

if the war had been shorter, and the post-war date earlier. We cannot in 1946 return to the conditions of 1939, not because of the war, but because of seven years. But when 1939, like 1914, is called 'pre-war', the ideas of either date, as well as the conditions, are given an appearance of antiquity which prejudices the freedom of discussion. It is right to have every morning a different opinion about the weather, but not about weather. These social ideas to which the improvisations of war have been favourable are liable to closure the debate on future policy by describing the suspended alternative ideas as 'pre-war', which we cannot 'go back to'. In fact, the main alternative ideas of economic progress have been so long in the field that we can hardly go forward on any side of policy without going back to some previous idea; it is by a very long splice that social ideas have ended in policies. We must leave it open for any methods to recur in economic policy, subject to changes in conditions caused by lapse of time.

It has been observed that many of the post-war plans, in 1918 and 1945, begin with the prefix re-, such as resettlement, reconstruction, recovery, and replacement. But the prefix is not used in a backward-looking sense; nor does it mean such a break with the pre-war conditions as to imply that a great war completely 'faults' the strata of national life. There must be an element of restoration, because it is absurd to suppose that the outbreak of a war, which might have been avoided, should exactly coincide with the due date for complete change of any economic or social arrangements. But a great and costly war does in some degree change the social outlook, partly as regards defects in social arrangements which may have been shown by the fact of war, partly as regards compensation for the human sacrifices

of the war, partly as regards the actual conditions created by the physical destruction or physical re-location caused by the war. The last of these may even be regarded as a sort of asset, in that it forces on a country plans for the rebuilding of cities which might have been delayed but for the clearance of the blitz. This is not the case, since the costs of rebuilding and re-location are given by war a forced priority over other uses of money, of perhaps greater urgency in an unforced consideration of the needs of all sides of the national economy. On the other hand, there is no problem of priorities if compensation for sacrifice quickens the whole search for social reform. But the net balance of all the plans which have the re- prefix is *at the best* some gain in time, which is low or negative interest on the human costs of war.

In the strictly economic account of the cost of war, the first item is the loss of manpower, and therefore of supply. This is also a deduction from the national demand. The population of a country may be more or less than optimum, by reference to its size, geographical location, and dependence on import of foreign materials. If it would have gained in facility of organization by a measure of emigration to foreign places, it does not lose, in strict economics, if the same lessening of manpower is caused by war; but this test would not apply if its emigrants went to its own dominions, with a preference for imperial trade. To a country which would have gained by immigration, war casualties are an economic loss. It is implied that the migrants in either case would have been as able-bodied as the war casualties. Annexations or losses of contiguous territories may better or worsen the result, according to the relation between the resources and the populations of the areas lost or

gained. The two wars have made this consideration important in Europe, but difficult to calculate, since optimum population is not a purely economic idea.

Apart from changes in population and manpower there is the question of the running cost of war to the population which carries it on. This is usually called the 'efforts and sacrifices' which that population has to undergo. But as regards the efforts, there is nothing particular to say. It is desirable that a nation shall be fully employed, and this happens in times of war. What they are employed in doing is a different question, but if there had been no war, they would have wished to be at the full stretch of their efforts all the same, that is to say, at full employment. What is the position as regards 'sacrifices'? This is the question of what people make by their efforts. They make fewer consumable goods, and more munitions or other war-time capital equipment. But if this is the choice of the nation, which in war regards munitions as having more 'utility' than some of its consumables, wherein does the sacrifice consist? At all times, some things are sacrificed in order to get other things; all choice is a question of priorities, and priorities are only a question of relative quantities. In time of war, there is a shift of these relatives; the margin at which expenditure on consumables and other things is regarded as equivalent includes more of the latter. It is this shift which represents the national sacrifice. Because, even if the new arrangement expresses the national choice in the conditions of war, it is a variation, imposed by these conditions, from the normal expenditure of the national income. If a nation always lived under the conditions of war there would be no background against which to measure the 'sacrifices', and they would be in the same category as the 'efforts'.

The sacrifices in consumable goods are a current cost of war, in the personal sense of cost. But they mean also a shift in the national equipment of the nation, which has partly been depreciated, and partly over-developed, against its normal uses in peace-time; and to this has to be added the destruction of useful peace-time property. This real cost has to be measured by reference to the trend of real income and investment as it existed before the war, and to the deficiency, after the war, of any elements of that trend. Or we can inquire how long it has taken after war to restore the real values of income and capital, against the pre-war values. Thus there would be shown a deficit of so much per cent in manpower, and so much per cent of capital, reckoned at pre-war values. Much of the capital created in war loses its value when war ends, because of its technical form or its location, and there is much depreciation of older capital; of course, some war-created capital has post-war value. But both manpower and capital assets are certain to be below the trend figures; much capital, in the form of foreign investment, has been turned into income and consumed. Thus, in the case of the Great War, it is stated by Bowley that two years after its close the conditions as regards material domestic capital had been restored to 1914 value; this was a loss of seven years of the trend. The same author shows that the real income position of an average citizen of this country had by 1924 reached the 1914 position in real values; so that his income loss was ten years of the trend. It will not be less than this for the second great war. The cost of war is thus reckoned by the difference in the economic strength of the country between the extrapolated pre-war and the actual post-war conditions.

The war-time change in the consumption of the nation

need have no lasting effect. The consumption in war-time is to a large extent collective, paid for by taxation and loans, in the form of munitions used up; in the last war, the 'private' consumption had to fall by about 20 per cent in real quantities. If the nation has been able to bear this reduction of what are mainly luxuries, and partly even deleterious articles, there is no lasting effect when the war is over.

The conception of the cost of war would be greatly extended if we had to include in it the cost of war preparation in time of peace, as well as the 'effects' of war on post-war economic conditions. As regards the first of these, the words of Hobbes may be quoted: 'War consisteth not in battle only, or the act of fighting; but in a tract of time, in which the will to contend in battle is sufficiently known. For the nature of foul weather lieth not in a shower or two of rain; but in a disposition thereto of many days together.' But a distinction should be made between the military cost of peace and the cost of war; and the expenditure on armaments in peacetime should be regarded as the cost of peace. It is intended that a strong military position will prevent a nation from having to go to war. The enormous difference in such expenditure between peacetime and war-timeshows this distinction; in 1938, in this country, it was 350 out of 4,600 millions of national income; in 1944, it was 4,500 out of 8,300.¹ Between 1815 and 1914 the expenditure on defence was a high percentage of the Budget, approximately one-third when the debt charge is included, but nearer a half if it is not included; but against the income of the nation it was a small charge, only 2 or 3 per cent, and this was so for a long period between the two great wars. Considering what is at

¹ Comd., 6623, p. 16.

stake if war breaks out, the cost of peace was kept remarkably low, so low as to require for it this special name; it depended on the behaviour of other countries, and a sufficient bargaining power. The cost of war is the cost of a new condition, and should be separated from the cost of peace. The peace-time expenditure on the forces has to allow for the rapid obsolescence of munitions and equipment, and much of it is for current services, so that war does not draw on an accumulated account. The post-war effects on employment and other economic conditions should also be kept distinct as effects, and not as costs of war. It is difficult to say to what extent they follow inevitably from a war, or to what extent they are avoidable by economic policy. There are aspects of peace-time policy which fall outside the sphere of direct military preparation, such as the protection of agriculture or other industries, with a view to the possibility of war; and the after-effects of war may be to strengthen them. It would be impossible to include all this in an estimate of the 'cost of war'. They are more nearly costs of peace.

Of course, all forms of peace-time policy which have war in view are not full 'insurances' against war. We do not, if war breaks out, get back from these peace-time outlays any important contribution to the cost of war. The idea that the cost of war was insured against by peace-time expenditure prevailed in the financial system up to 1914. It was thought that a large sinking fund created a tax reserve which could be transferred to military expenditure on the outbreak of war. But the difference between the costs of war and of peace was soon made plain, since the sinking fund of 1914 could not have kept the war going for even a week of its first year. It was also thought that a low income tax created a

further reserve, since it allowed a larger margin for increased rates during war; a rate of one shilling was stated to be excessive in 1913, for that reason. This idea of a war reserve of direct taxation, in a free trade country, obstructed the free development of expenditure on social services, and was a complete fallacy, since the rates of taxation in war depended solely on war-time needs, and would have been the same whatever had been the rates during peace. There was no accumulated financial reserve, only a shift in the purposes of expenditure. On the other hand, the protection of fundamental industries, specially of agriculture, does create an accumulated reserve of fertility or of skill which is more nearly a real insurance.

The increase of the domestic debt of a country is not a measure of the cost of war. What it shows is, how much of the money cost has been met by borrowing instead of by taxation. Borrowed money, since it was obtained, could have been obtained by some extreme device of taxation, but the tax system would have had to be so discriminative between large and small incomes as to be unworkable. Part of the domestic debt has been caused, in this country, by the sale to the government of foreign investments, against the creation of domestic debt; this affects the capital strength of the country, and the reduction of foreign investments enters into the real cost of the war. But if we also took the increase of domestic debt into the cost of the war, we would count twice over the loss of foreign investment. The availability of large foreign investments which can be realised in war, does not mean that the 'sacrifices' of war have been those of previous decades, but only that they have given the war generation an asset by which it can spread the burden of its own sacrifices. But the increase of

domestic debt is an important aspect of the effect of war. After 1815 until 1880, the charge for the service of the debt exceeded the military expenditure of this country; it fell between 1901 and 1914 to an average of one-third of this, and after the Great War it exceeded it again. Between 1921-2 and 1934-5, it averaged three times the direct military expenditure. It affects the level of taxation to the full effect of its face value, but this part of taxation is usually referred to as 'transfer' taxation, while expenditure on current supplies is defined as 'onerous'. How does this distinction bear on the question of the effects of war? The belief that a war debt throws a burden on posterity has been instinctive in ordinary opinion; Hume, Smith, Ricardo, and Jevons were among economists who argued to the same effect. In recent times, the 'transfer' argument has been more prominent.

Taxation is described as 'onerous' if it uses up national resources. This is a rather strange opinion, because it is the purpose of resources to be used up. Labour is one of the national resources, the use of which is employment. Is it not more proper to argue that the taxation which is applied in making use of national resources is the taxation which really fructifies, and ought to be encouraged? On the other hand, taxation which only transfers money from the rest of the community to the fundholders seems to use up the time of money without any productive result. Now, all taxation, and especially high taxation, is deterrent of enterprise and investment. That part of a high tax which is applied in using up our resources of labour and materials offsets this deterrent influence by its contribution to production of goods or services; but that part which is only applied in transferring money has no such offset to its deterrent

influences. It is the latter, rather than the former, which should be described as onerous to the national economy.

It is true that the interest on the debt is itself taxable, and that the State 'gets back' a considerable levy, which is greater the higher the rate of taxation. This is no mitigation of the position. The State also taxes what it pays to public servants of all sorts, and so 'gets back' some of what it pays to them; this does not in the least change the fact that the whole tax is effective as a tax to its full amount. It means only that fund holders are part of the nation, who derive, like others, advantage from the security obtained from the expenditure of war loans.

It has been held, on the other hand, that the transfer of the interest on the debt is from the poorer to the richer, or from the more industrious to the more idle, or from the younger to the older parts of the nation. This has not been shown. It is even held that the transfer may be nationally advantageous according to the way in which the debt is held, so that if the poor held most of it there would be a net advantage. But those who hold most of the debt must have subscribed it, it was not bestowed upon them. During a war, the investor in the funds is appealed to as a patriot, but after war becomes a 'rentier', for whom there is a treatment now called 'euthanasia'. All these are confusions of the argument, the essence of which is that transfer expenditure is an unfruitful tax, and is therefore a burden on the country.

Another financial effect of war is that it is liable to cause large future expenditure to be more lightly regarded, because the high rate of public expenditure during the war lowers the significance of any given sum of money. Thus, when a post-war proposal is being considered,

which would cost 200 millions a year, it can easily be said, as it has been, that this is only a fortnight's cost of the war; so that the more expensive the war, the less the motive for future economy. The difference between a single war-time outlay, and a recurring future outlay is overlooked. Since war-time expenditure is financed largely by borrowing, this line of thought is apt to make 'deficit finance' into an ideal of policy, without proper discrimination of the purposes of borrowing. It is obviously quite proper for a government to borrow for purposes of reproductive capital outlay; social policy decides whether in particular cases this is to be done by the government or by private concerns; the nationalization of industries will transfer this function to the State. It will require a separation, in the annual accounts, of capital from income transactions. 'Deficit finance' is not in the same position when the government borrows for the sake of current expenditure on social schemes, such as allowances or subsidies, which create no real additions to capital. It appears now to be accepted that the Budget should balance expenditure against taxation over a period of years, but not necessarily every year, in order to control the creation of deadweight debt. This is not a new idea, though it has a larger scope. This kind of deficit finance has to take place in war-time, when capital is borrowed for consumption in munitions, and it is the scale on which this happens which is liable to demoralize the idea of economy in peace-time, and to make the balanced Budget seem 'pre-war' and out of date.

The methods by which a growing population holds off the problem of scarcity are invention, discovery, organization, and what may be called 'application' or

'stimulus'. Those who regard war, despite its human sacrifices, as an element of progress, may refer to its influence on these methods.

First, as regards invention. There may be technical inventions in the machinery and art of war itself, and the history of war shows how rapid they are; for war cannot be rehearsed or fully prepared for. Those who have been in the field during the last two wars know how complete in a few years has been the transformation of their technical equipment, for offence and defence. Such inventions, if their use ends with the war, are plainly to be ruled out of this argument. As a rule they increase the post-war cost of peace.

The pressure of war may cause the invention of technical methods, which had not previously been perfected or applied, and which are permanent improvements on pre-war methods. It has proved to be difficult, if it is possible, to find a clear case of this. The fields of service in which to look for such cases are the chemical, metallurgical, and electrical; but research seems to show that the contribution of war has been that it has created a sphere for projects already known, rather than entirely new scientific projects. The beet-sugar industry in Europe was the result of the Berlin Decrees in the war with Napoleon; this is perhaps the largest instance that can be quoted, though the discovery of sugar in beet dates from 1747 and a factory was first set up in Siberia in 1801. In other notable examples of the influence of war, what appears is a special opportunity for increasing the pace at which pre-war projects have been made feasible.

If we examine such cases as synthetic products, substitute materials, atomic energy, radar, or jet propulsion, it appears that war gave a great impulse to the furthering

and application of what science had already had in project. In 1911, synthetic rubber was regarded as a pure speculation, for the reason of its cost; in the First World War, Germany was forced to develop it as a military proposition, and it was available for commercial use in that country in 1936; by 1938 some varieties of it were thought superior to natural rubber; in 1944 its production was two-thirds that of natural rubber, but its cost was much higher.¹ During the war, Germany developed the production of nitrate from the air, so that from 6 per cent in 1913 it became by 1928, 70 per cent of the world output of nitrate. Radio detection dates from 1884, when it was discovered that radio waves were reflected from solid objects; a patent was taken out in 1904 on a proposed method of using this property as a navigational aid for ships; Marconi revived the idea in 1922. The principle of pulse ranging, which characterizes modern radar, was first used in 1925, and its developments thereafter were mainly made for the purpose of military use, and the defensive detection of aircraft. Its progress in the last war was phenomenal; 'probably no scientific or industrial development in the history of the world has expanded in all places simultaneously on such a scale'. Its contribution to progress is its peace-time use, and its influence on the methodology of research; the requirements of war have hastened its contribution to navigational safety against night or weather, but still more 'the impact on electronics generally of techniques developed during the war because of radar will have profound and far-reaching effects on the shape of our daily life'.² The release of atomic energy had been a scientific pursuit for nearly

¹ Enc. Brit. Text Book, 1938, 1944.

² *Radar*, H.M.S.O., 1945.

a generation, until the last war placed unlimited resources at the disposal of faster research. The discovery of synthetic or substitute materials is due to the fact that nature does not have in view man's industrial requirements, and that natural products are in many ways deficient or alloyed in regard to these requirements; in respect of crops and animals, we can make her breed differently, but in inorganic supplies the chemist has to treat her products with the new technique of synthetics. In this field there has been a long course of research, the first ideas or patents being pre-war. War increases the tempo of technique and application, because there is no question of commercial profitableness, and unlimited funds are placed at the disposal of research and application. Some of this new inventiveness is retained in peace with a view to any future war, and substitute products may therefore be maintained by protection against cheaper natural products; this is not a clear contribution to progress. It does not fight scarcity. But some substitute products are commercially suitable on their merits for some purposes; and there is always the reserve of scientific knowledge which they create, against any change in natural conditions of supply. Further, there are two reactions: first, in respect of war-time activities which are closely related to peace-time activities, as military aviation is to civil aviation; second, in respect of war-time purposes which affect the methodology of the processes applied to them, of which radar is a special example. 'War-time advances, such as the general introduction of the improved puddling and rolling processes gave the British iron industry a decided superiority over their continental rivals after 1815.'¹ In such cases we have the 'key' industries acting in

¹ Redford: *Economic History*.

reverse. A key industry is maintained in peace, not solely because of the importance of its product, but because its processes and technical methods can be adapted to a war-time purpose; this is the reason, at first seeming remote, why the dyeing industry was specially maintained in this country. But in some cases, it appears, a war-time result has been the key to a peace-time development. On the other hand, whatever residues of war-time inventiveness are left over as contributions to peace, these visible results in some industries have to be offset by the war-time delays in invention in other industries not of primary war-time importance, so that their inventiveness is for a time atrophied. The development of rayon was checked by the Great War. The gains are more visible than the losses.

Although so many war-time inventions are mainly of war-time utility, the expanding rate of progress in such fields as radar, jet-propulsion, and atomic energy shows how great are the inventive powers which are always latent, until they can be realised by sufficient expenditure on research. The reflection cannot be escaped that there must be a great lag in the application of fundamental research which would be of great national advantage, since the war has proved the high elasticity of inventiveness when it is liberally endowed. This is perhaps the most important lesson we have been taught by the inventiveness of the war years.

It should also be observed that, for a more accidental reason, the use of the pre-war results of research may be, and is thought to have been, enlarged by the break-up of restrictions imposed by the holders of patents. Under private international arrangements, there were many cases of such restrictive conditions imposed from one country upon the users of its patents abroad, in order

to maintain both the economic and the military advantage of the former. The cartels or other arrangements on which these restrictions depend are broken up in war.¹

The influence of war on progress through the factors of discovery—the opening up of new sources of supply—cannot now have the same elasticity as in the case of invention. In this century, wars in Africa, China, and Abyssinia have had this motive, or retrospective sanction; they are called ‘civilizing expeditions’ against backward natives or peoples, whose backwardness may be held to be impeding world supplies. ‘A State’, said David Hume, ‘can scarcely carry its trade and industry very far, when the surrounding States are buried in ignorance, sloth, and barbarism.’ And, much later, ‘One can guess’, said Lord Bryce, ‘what would be the fate of any weak community in which radium was found in abundance.’² There is some reason in the view that every country cannot be allowed to live its own life in its own way, if it fails to develop resources which the world requires; and the ‘native’ peoples against whom the ‘peripheral’ wars of last century were fought did not understand this sort of argument. The accusation of ‘exploitation’ is answered by the defence of ‘development’, since the land of the world is limited while its population increases. How much sacrifice of life the pace of development is worth is an ethical question; ‘life’ lost in one sense is compared with ‘life’ gained in another sense. The absolute command of Kant’s ethics, ‘never to use other persons as a means only, but always as an end’ is appeased by the civilization which, it is claimed, follows on exploitation. The moral of wars of

¹ Many instances are given in the T.N.E.C. Reports of the U.S.A.

² *International Relations*, Lect. III.

exploitation takes a second form when countries so opened up and civilised *then* desire, on that new level, to live their own lives in their own new way, as for example the Javanese or Indians do now. The white man's burden can be taken up and also thrown off, and this aspect of the history of war might come to be closed in our time with a carefully reasoned retrospective favourable economico-ethical verdict.

Lastly, what is the contribution of war to progress in the organization of the economic system?

War practically abolishes unemployment. The figure reached in the last two wars is indeed far below what has been held to be the amount of unemployment which is necessary for the mobility of labour in peace-time; since absolutely full employment would mean that no one could move from one job to another job that was vacant. When labour is 'directed' this objection to full employment ceases to apply, since the government arranges the movement; unemployment could therefore fall below 1 per cent. This fact is not a contribution to the employment when controls are removed. But it has been held that the experience of war shows that, with proper application to the problem, employment can always be kept as 'full' as the mobility of the system requires. The conditions of war, however, are that the government compels the people, through taxation and borrowing, to buy at cost whatever it orders to have produced; there is no question of consumers' choice or of commercial values. In such conditions, the creation of employment is fool-proof. An entirely new problem is created when market demand is restored; and the methods which have then to be adopted require a new argument and a new method. The question, 'if we can

have full employment in war, why cannot we have it in peace?" is not well put, and overlooks differences as fundamental as they should be obvious. In war, the control by the State over employment is dominant and regardless of economic values; in peace, it is supplementary to a system in which economic values are dominant. There is all the difference in the world between these two sets of conditions. It is not a practical lesson of war that government could abolish unemployment in peace by employing people in making just anything, taxing them for the cost of making it, and relieving the accumulation of stocks by continuous demolition. But if employment, as well as production of values, is one of the things that industry is for, the products of the public work which is arranged so as to fill the gaps of private work may be more vaguely valued, as contributions to welfare, than the market would value them as contributions to wealth. If, however, the post-war world urgently requires the greatest contribution to real wealth, public work must contribute to that as well as to welfare, and the new framework of the problem of employment has a new aspect, to which the tax-debt-demolition methods of war do not contribute much. The official announcement (May, 1946) that there is to be 20 per cent of public industry and 80 per cent of private industry just reverses the war-time conditions.

The full employment of war-time disguises the future problem of employment for another reason. Projects of employment require assurance of the materials of production, which in this country have mainly to be imported. Allies in the war effort are willing to send these supplies, on an account not to be settled till the war is over; and foreign assets can also be sold against

imports. In peace, the problem of full employment has to be solved in the absence of such subsidies to employment; to say straight off that what we have done in war we can, for other motives, do in peace is too quick a conclusion; to have full employment we must, indeed, do something else in peace than we have done in war, namely, meet the foreign obligations which must be contracted in order to supply the means of employment.¹ Public schemes of work to fill a threatened gap in the private market for work must be assured of their material requirements through the efficiency and volume of the export trade. Domestic borrowing, or deficit finance, does not by itself give this assurance; if a million pounds are borrowed, it depends whether the exports bought here for that million will sell abroad for the foreign cost of their own imported materials, plus the materials required for the public works whose products are not exported, such as houses, and other domestic improvements. This peace problem is plainly quite different from what happens in the unsettled accounts of war-time.

These questions of what a period of war can teach us as regards full employment are of course separate from other aspects of the actual effects of war on employment. The amount of industrial unsettlement, and the period required for revival, depend on the magnitude and destruction of war. In this country, unemployment after the First World War was two and a half times what it had averaged before that war, for fifteen years. Markets are changed by war, and policies are changed also, and foreign trade has new conditions. Our abandonment of free trade and the gold standard does not permit a clear argument on the merits of these principles, by

¹ Marshall Aid has suspended this question for a time.

comparison of the pre-war and post-war levels of unemployment, because of the jolt which the whole economy had sustained in four years of war. Six years of the second war have even more fully altered the conditions to be considered for future policy; if post-war unemployment falls as much as it increased after the first war, that will be because of better policy, and the two wars will cancel each other in any argument about war itself; if there comes another economic blizzard, they will reinforce each other.

It is very doubtful whether the experience of war has contributed anything to the question of the organization of capital. In a long war, there are improvisations which, at first intended to last 'for the duration', became so inset that there may be a question whether 'returning were as tedious as go o'er'. This has applied particularly to the official controls, so as to affect the argument for the nationalization of some fundamental industries. There has also been the experience that highly combined industries are easier for the State to take over and control in emergencies. Therefore, after the First World War, a series of reports urged on this country a change of opinion about high monopolistic combinations in industry. But, while the duration and magnitude of the last two wars, especially the second one, have created some strategic advantages for arguments about monopoly and nationalization, these arguments had been quite well advanced in peace-time, and the wars did little or nothing to change their trend. All such argument should be futurist instead of retrospective, and the retrospect on war controls and organization has affected opinion as much in one direction as in the other. Even those who wish to confirm the war-time improvisations of control on the side of capital wish to undo them on the

side of labour, and to 'restore' Trade Union conditions.

In a number of ways, war 'faults' the trend of national development; this is obvious as regards prices, taxation, debt, and employment. It probably does so also in respect of real capital resources at home, after allowance is made for such war-time constructions as continue to be wholly or partly peace-time assets. As has been said, the mere restoration of a pre-war position means the loss of time during which any trend would have moved. Of the French War, it has been said that 'it was not until the second quarter of the nineteenth century that the direct effects had been shaken off';¹ the two wars of this century seem to suggest ten years, or five after the peace, as the possible dates of restoration. This, with the loss of life, and the immaterial losses, is sheer cost of war. On the other hand, war is apt to 'fault' the course of opinion, by establishing an artificial and pretentious contrast of the post-war with the pre-war, which means the post-war intentions against the pre-war facts, and much bravado of argument is thus created. The gold standard, free trade, and private enterprise were pre-war in 1920, but in 1946 the opposites of the first two of these were pre-war; and in that year, the 'new economics' was also pre-war. Pre-war argument is, in fact, very selective. The trend of thought is not so completely broken that methods of policy once tried cannot in new conditions be tried again; even if a gold standard or free trade were restored, the fluctuation of opinion about them has been such that words could easily be eaten again with good table manners. It is future, and not past, conditions which will decide these things. It has been argued above that, as regards opinion on organization, the trend of argument has continued; the wars have not

¹ Redford: *Economic History of England*.

contributed much. The nationalization of some fundamental industries would have occurred whenever a Socialist government was in power, a result which the last war may have either hastened or delayed. It has always to be remembered that dates other than war dates could just as well be quoted in such comparisons; great changes in social policy as regards education, wage policy, and employment policy have had their own dates, to determine their 'before' and 'after'. There is pre- and post-Lloyd George.

Finally, there is the spirit of 'application', to which a special contribution is claimed for war. Some new organizations were created in war, like the Whitley Councils or the Department of Scientific Research; but most were not. It was this spirit of application to the problems of the nation which led the economist McCulloch to say that 'but for the contests in which we have engaged since the Revolution, the greater part of the wealth expended in carrying them on would never have existed', and led Coleridge to argue that it was our National Debt which was the true cause of the defeat of Napoleon. Obstacles, it is argued, call for efforts which more than overcome them. Peace is not lacking in any opportunities of this kind, such as Peel offered to the nation in asking for the then extreme effort of the income tax, or as the author of the 'War Budget' of 1909 proclaimed. We have only had two great wars by which to test the generalities of highly pitched hopes and promises, and one of them failed. The second is in the throes of begetting we do not know what, till the application called for is tried against the strain of its endurance.

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