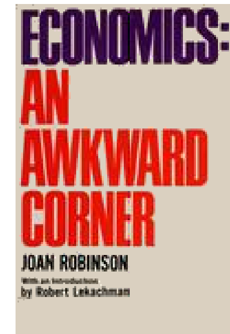
JOAN ROBINSON

ECONOMICS

An Awkward Corner



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PREFACE

This book was being written in the summer of 1966, when current happenings provided a painful illustration of its main thesis. I do not think that there is much hope that events while it is in the press will prove it wrong.

Some quasi-technical terms are italicised where they first occur and their meaning is indicated.

Notes which contain some argument or information are numbered. Those which are only references are marked by letters.

JOAN ROBINSON
August 1966
Cambridge

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INTRODUCTION

It is impossible to understand the economic system in which we are living if we try to interpret it as a rational scheme. It has to be understood as an awkward phase in a continuing process of historical development.

No doubt in every age economic life has been a scene of conflict and compromise, defended by rationalizations that did not fit with experience. Fifty years ago, Sunday-school children were taught to sing:

> The rich man in his castle,
> The poor man at his gate,
> God made them high and lowly
> And ordered their estate.

In this century, the conflicts are more acute, the compromises more uncertain and the rationalizations more unconvincing because history has been going on so fast.

Keynes described the capitalist economy before 1914:

'Europe was so organized socially and economically as to secure the maximum accumulation of capital. While there was some continuous improvement in the daily conditions of life of the mass of the population, Society was so framed as to throw a great part of the increased income into the control of the class least likely to consume it. The new rich of the nineteenth century were not brought up to large expenditures, and preferred the power which investment gave them to the pleasures of immediate consumption. In fact, it was precisely the inequality of the distribution of wealth which made possible those vast accumulations of fixed wealth and of capital improvements which distinguished that age from all others. Herein lay, in fact, the main justification of the Capitalist System. If the rich had spent their new wealth on their own enjoyments, the world

would long ago have found such a regime intolerable. But like bees they saved and accumulated, not less to the advantage of the whole community because they themselves held narrower ends in prospect.

The immense accumulations of fixed capital which, to the great benefit of mankind, were built up during the half century before the war, could never have come about in a Society where wealth was divided equitably. The railways of the world, which that age built as a monument to posterity, were, not less than the Pyramids of Egypt, the work of labour which was not free to consume in immediate enjoyment the full equivalent of its efforts.

Thus this remarkable system depended for its growth on a double bluff or deception. On the one hand the labouring classes accepted from ignorance or powerlessness, or were compelled, persuaded, or cajoled by custom, convention, authority, and the well-established order of Society into accepting, a situation in which they could call their own very little of the cake, that they and Nature and the capitalists were co-operating to produce. And on the other hand the capitalist classes were allowed to call the best part of the cake theirs and were theoretically free to consume it, on the tacit underlying condition that they consumed very little of it in practice. The duty of "saving" became nine-tenths of virtue and the growth of the cake the object of true religion. There grew round the non-consumption of the cake all those instincts of puritanism which in other ages has withdrawn itself from the world and has neglected the arts of production as well as those of enjoyment. And so the cake increased; but to what end was not clearly contemplated. Individuals would be exhorted not so much to abstain as to defer, and to cultivate the pleasures of security and anticipation. Saving was for old age or for your children; but this was only in theory—the virtue of the cake was that it was never to be consumed, neither by you nor by your children after you.

In writing thus I do not necessarily disparage the

practices of that generation. In the unconscious recesses of its being Society knew what it was about. The cake was really very small in proportion to the appetites of consumption, and no one, if it were shared all round, would be much better off by the cutting of it. Society was working not for the small pleasures of today but for the future security and improvement of the race—in fact for 'progress.'' [a]

Writing in 1918, Keynes thought that the war had smashed this system up, but it staggered to its feet again. Not the war, but the great slump of the thirties struck the mortal blow. It is painful to reflect that, if a British government after 1931 had known how to make full employment by peaceful means, the Nazis would have had no appeal. But full employment, in the democratic countries, had to wait for a new war, and ever since, cold and hot wars have made a great contribution to maintaining it. The Western world learned by the collapse of the market economy (from which the Soviet Union was immune) that the cake was already large and that when it is not cut it dries up and crumbles away. But we have no philosophy to guide us in sharing it out. The old hymn throws the glamour of feudalism over inequality. It did not say:

> The rich man in his board room
> The poor man in his slum.

Now what story are the children to be told?

It is impossible to imagine the huge accumulation that made modern industries possible without the 'double deception' of bitter exploitation on the one side, and devoted profit seekers on the other. Social justice and political equality would have strangled the system before it could grow. The institutions and the habits of mind built up during the period when the surplus was being squeezed out survive after they have ceased to be useful and have not yet been replaced.

The notions of *laisser faire*[1], that business men know what is best, are contradicted by the evident need for planning to maintain 'a high and stable level of employment.' The notion that property confers obligations to justify privilege is contradicted by the separation of ownership from control in modern business. The notion that governments have only to see fair play between employers and employed is contradicted by the requirements of control over money incomes and prices. The notion that the free play of supply and demand produce a viable system of international trade is contradicted by the payments crises from which no country is immune for long.

These contractions arise from the need to readjust the organization of Society to the fantastic capacity for production of material wealth that the application of science to technology has made possible.

Such problems arise within the Western industrial nations. Meanwhile, their situation in the world has changed still more dramatically. They are now rivalled by socialist nations which have installed modern industry far more rapidly than they did themselves and surrounded by a third world where misery is growing faster than wealth. These internal problems, however, are matter enough for this little book.

I

INCOMES AND PRICES

THE economic problem that bites most nigh to every citizen is the problem of rising prices. In the last fifteen years money incomes, overall for the country as a whole, have risen more than prices; what is called consumption in *real* terms (the value of purchases of goods and services divided by an index of prices) has increased substantially.[2] But the rise in real incomes has been arbitrarily distributed amongst families. Some are much better off, many have gained little and some are even worse off.

Generally it is those who are in any case in a weak position who suffer most as the prices of what they need to buy rise faster than their incomes—ill-organized workers, pensioners, widows and orphans who have been left with fixed-interest securities. Moreover, prices rise more or less continuously while the income, from wages, salaries or social security benefits, of any one group rises only at intervals. At a particular moment, the majority find that their real income has fallen since last year while a few, whose pay has recently gone up, are enjoying a temporary relative advantage. The other side of the coin is the gain, at the expense of their creditors, to government and business who have obligations fixed in terms of money, and the 'unearned increment' of wealth dropping into the laps of those who happen to own particular pieces of land or works of art fashionable with the dealers.

The old doctrine that once inflation starts it is bound to go all the way to total collapse has been discredited. The economy adapts itself in various ways to the expectation of a gradually falling value of money. For instance, the widows and orphans now invest in equities whose money value rises (if they are well chosen) with prices. The law is amended to permit this and new institutions such as unit

trusts are created to enable them to spread their risks. The leap-frog game of rising incomes spreads from the trade unions to the professions. Those are are in the strongest position protect themselves; those who suffer most are the least articulate. Thus inflation nowadays does not get such a bad press as it used to do.

The most powerful objection to inflation is not that it is cruel, tiresome and demoralizing at home but that it is destructive in international competition. A country which is in any case in a weak position is driven to desperation when (with a fixed exchange rate between currencies) its costs are rising faster than those of its competitors. It is for this reason that it has become a prime object of policy in this country to check the rise of prices.

PRICES AND COSTS

The relation between wages and prices is often stated in a vague general way. Wages are the largest element in costs and an important element in demand, so that if money-wage rates rise, prices of commodities are bound to rise also. At the same time, higher prices raise the cost of living, setting up a demand for higher wages, and so the vicious circle is joined.

The relation of prices to wages can be analysed more exactly. The prices at which goods are sold to the public, generally speaking, are set by the firms which produce them. Prices are governed by costs, but costs are not a simple concept. *Prime* costs—wages, materials, power etc. —vary more or less directly with output week by week, and the *overhead* expenses of running the business, the upkeep and depreciation of plant, and net profit have to be recovered from a year's output. What average cost per unit of output will be has to be estimated in advance on the basis of an estimation of what output will be sold.

The usual method of forming prices is to add to prime cost a percentage *gross margin* calculated to yield whatever net profit it is reasonable and safe to aim at.[b] Wholesale

and retail margins are added to the producer's price. Thus the whole structure of prices is based upon prime costs. Apart from his own wage bill, each producer's prime cost consists of payments to others, which in turn cover prime costs with a margin, so that, apart from imported raw materials, prime costs are governed by wage costs. Thus a general rise in the level of money-wage rates leads to a more or less proportionate rise in prices. The money to buy the goods at higher prices is provided by the higher wages and the higher profits that accompany them and so, apart from foreign trade, there is no check upon the process.

There are other influences on the general level of prices. Moderate swings in demand generally affect output, leaving margins unchanged, but a sharp increase in overall demand (such as may come about when there is a cut in taxes or an increase in expenditure on investment or armaments, which generate income without providing anything for it to be spent on) creates a *seller's market* for a number of industries, in which the output that could be sold with the normal margin is greater than can be produced with existing capacity. Some meet this situation by lengthening delivery dates but some meet it by raising prices. Thus an increase in demand ahead of an increase of capacity to provide for it is liable to raise prices relatively to money-wage rates.

The prices of raw materials which are sold in competitive markets are not subject to the mark-up system, and vary sharply under the influence of supply and demand.[c]

Moreover, margins are not completely rigid. There is a general tendency for an upward drift in margins, for where a line is profitable *non-price competition* sets in, by advertising and sales pressure of various kinds. As with an armaments race, selling costs undertaken by one competitor force others to reply, so that all find their costs have gone up, and prices have to be kept high to cover them. (When you buy a packet of goods, you are contributing to the cost of

persuading you to buy it.) On the other hand, a competitor will occasionally break into a market with a new method of selling and bring margins tumbling down. At times, also, for reasons of long-term strategy or in response to public policy, a group of firms may keep prices constant, allowing margins to shrink, when wages rise, 'absorbing', as they put it, the rise in costs.[3] When this happens on a wide scale, the sellers are agreeably surprised to find that profits per annum do not fall, for spending by the public has not been cut, and with higher real incomes they are buying more goods; overall, the increase in output sold more or less compensates for the reduced profit per unit. The effect, of course, is not spread evenly. Some sellers lose while others positively gain.

Increasing productivity has a general tendency to reduce prices. Investment increasing the stock of productive capital, technical improvements and the entry of new commodities into mass production, raise output per man employed, and so, at given money-wage rates, reduce costs per unit. Provided that an upward drift of margins does not cancel the benefit, the effect of rising wages on prices is thus mitigated.

Influences such as these, which play upon the relation of prices to money wages, may have an important affect on real wages, but their influence upon the absolute level of prices is limited compared to the influence of wage rates, for they can influence only the proportion of prices to wages, while wages can be multiplied without limit.

Trade unionists often object to rising wages being blamed for rising prices. Why pick out wages? What about other incomes? But it is not a question of anyone behaving badly according to the rules of the game. When prices rise it is right and proper for workers to demand a rise of wages, and this prevents prices from relapsing again. When wages rise, it is normal for businesses to raise prices, not by the amount but by the proportion in which prime costs have gone up. When the incomes of one group are raised it is

perfectly proper for others to ask for as much. When there is a high level of employment overall there is an acute scarcity of labour of some particular skills or in particular districts. Efficient, go-ahead firms, which can see a profitable market if only they could get more hands, attract labour by offering various inducements over and above the standard wage rates (such as overtime on Sunday with a day off on Monday). *Wage drift* due to this competition may lead rather than follow trade union demands. From time to time a revision of standard rates puts a rachet below the level to which earnings have drifted since the last bargain was made. To expand sales in a profitable market is the first duty of a business, and to catch a share of the profit for its members is the first duty of a trade union. No one is behaving badly. It is no one's fault. It is how the system works.

A NEW ORTHODOXY

The proposition that, in an industrial economy, the level of money-wage rates governs the level of prices was an essential element in the analysis of Keynes' *General Theory of Employment, Interest and Money*, published in 1936. The part of his argument which concerned the need for government policy to maintain 'a high and stable level of employment' was accepted into the canon of received orthodoxy in this country even before the end of the war in 1945 but the part which concerned wages and prices was resisted much longer. It was easy to predict that if we stumbled into near-full employment with institutions and attitudes unchanged, the balance of power in wage-bargaining would tip in favour of the workers, so that a vicious spiral of wages and prices would become chronic.[4] Yet it took about fifteen years of experience for the point to really sink home. Many professional economists and most Chancellors of the Exchequer continued to maintain that the movement of prices was something to do with the management of the monetary system.

Perhaps the idea that the value of money lies in relations between people, not in a solid, objective standard against which individuals can measure themselves, was a greater blow, even than the idea of employment policy, to the complex of vague but powerful traditions inherited from the heyday of laisser faire. Moreover monetary policy can be presented as a technical matter to be left to 'experts' without bringing conflicts of interest sharply to the surface. And the plain man, who prefers to think in simple terms of right and wrong, did not like to be told that two good things, full employment and stable prices, might be in conflict with each other.

However, that may be, a new orthodoxy has at last become established, and now the cry is all for *incomes policy*.[5]

INCOMES POLICY

There is one school of thought which contends that, since the trouble arises from near-full employment, let us give it up. Supporters of this view maintain that a 'moderate' amount of unemployment, say between two and three per cent over all, would be sufficient to keep wages in check and secure stable prices.[d] The evidence for this view is very sketchy. It might need much more. But, in any case, deliberately to adopt such a cold-blooded policy is out of the question. Even the deflationary measures of July 1966 were *intended* to bring only a temporary increase in unemployment as a side effect of redeployment of labour between industries. For incomes policy reliance was placed upon a freeze of wages.

Incomes policy is an expedient to cope with a pressing situation. There is no articulate philosophy behind it. The philosophy which it implies is both a rejection and an acceptance of laisser faire. It emphatically rejects laisser faire, since it expresses an acknowledgement that the free play of the market does not establish an equilibrium price level, rather a progressive degeneration in the value of money. At the same time it tacitly accepts the distribution of real income that the market throws up.

An ideal policy for stable prices (leaving the international aspect aside for a moment) requires the general overall *average* of money wage rates to rise at the same rate as the general average of output per head, and it requires the *average* of prices to be constant—falling for the most progressive industries and rising where productivity fails to rise at the average rate. (All these averages are more or less roughly expressed by index numbers which cannot be perfectly precise, so that even the ideal is not quite unambiguous.) Such a programme entails constant profit margins and a constant share of wages in the proceeds of industry (when the overall ratio of capital to output is not changing appreciably); capital then receives its share from a constant overall average rate of profit on the gradually growing total of capital invested. This implies that the share of wages in the value of output is acceptable.

Such a philosophy was at one time consciously and articulately adopted in Holland. The economists worked out the percentage change in national income every year, and the trade unions agreed to the same percentage rise in wages. (After working successfully for some time, putting Holland into an excellent competitive position in international trade, the policy was eroded by the demand of expanding firms to be allowed to compete for labour and finally had to be relaxed because higher wage rates in Germany were attracting labour over the frontier.[e])

The British labour movement was built up through a struggle for a larger share of the cake, and whatever its knights may privately believe, they cannot openly surrender and agree to the laisser faire doctrine that the 'factors of production' each get just what they deserve.

Nor would it be merely a verbal surrender. Certainly *most* of the benefit of raising the general level of wage rates is lost through rising prices, but not quite all. If pressure on wages were relaxed, it is very likely that falling costs

due to increasing productivity would be 'absorbed' the other way round, prices being held more or less constant and margins allowed to rise. The proper *quid pro quo* for wage restraint is cutting prices in the more progressive industries.

Even this is not at all satisfactory from the trade-union point of view. Workers are interested in the prices of what they buy, not of what they produce. The employees of each business want their own business to be profitable and to share in the swag, no matter whether the profits are monopolistic or not. How can the overall bargain be implemented when, in each particular case, neither side has an interest in fulfilling its terms?

Moreover each group of workers feels that they have a right to expect some benefit from increased efficiency in their own industry. Indeed, the best hope of getting British industry out of the doldrums is to enlist the workers in the cause of improving productivity, not only by eschewing restrictive practices and senseless demarkation disputes, but by actively co-operating with management, and spurring it on, to reduce costs. Incomes policy is often proclaimed in terms of limiting the rise of wages to the rise of output, as though each occupation should be rewarded for its own productivity. Relative differences in the proceeds of different branches of production and trade are partly due to differences in the personal efficiency of the workers concerned, but much more they are due to the luck of the draw in competing for market demand, in the technical conditions of particular lines of production, and in the energy and skill of management. Workers in the less progressive industries are not to blame. The basic principle of the market system is that the benefits of progress are passed on to the community as a whole, not bottled up in the industries where they happen to arise. A wage system based on differential productivity would prove unworkable even before it began.

These difficulties are concerned with the overall distribution of income between work and property. There are great difficulties also arising from the relative earnings offered by various types of work. The valuations which society puts upon different occupations are highly arbitrary. They have their roots in a long past history. In an era of near-full employment and growing educational opportunities, supply and demand work upon them, but the market works very sluggishly. Conscious policy is needed to remedy anomalies which threaten to dry up recruitment to some necessary service—say coal miners or school teachers. But once we begin to think about it, what is not anomalous? The whole affair seems to correspond very ill with our notions of justice and morality.[f]

Overlaying all this are the anomalies introduced by the very process of inflation. The leap-frog system by which rates of pay are raised for one group after another leaves always some one who is due for a rise. To start off fair with incomes policy, the tail should be allowed to catch up while the head of the line is held still. This is admitted in principle, but very imperfectly applied—the judges found it easier to catch up than the seamen. To enforce overall restraint, beginning at any particular date, leaves many rankling grievances behind, and the trade unions are put into an impossible position when they are required to administer a policy that their members feel to be unfair, and which indeed is so.

The problem of prices under full employment brings sharply into focus the contradictions of modern capitalism. However, a perfect incomes policy is, in any case, a Utopian scheme; rough and unfair as it may be, it may succeed in slowing down the rate of rise of costs relatively to those of other industrial nations, so as to give this one a better chance in international trade. This, far more than any search for social justice, is its primary aim.

II

THE BALANCE OF TRADE

THE problems of international trade lie deeper than relative rates of inflation. There is no particular reason to expect trade for each country to balance in a market economy. Nations, in various shapes and sizes, are formed by history and geography without any regard to economic convenience. As population grows and tastes and technology change, the pattern of demand and supply of various goods and services in the trading world is constantly shifting; at any moment the inhabitants of one patch of the earth's surface find that their resources, natural or accumulated, their skills and inventiveness, their market connections and business acumen, make it easy to sell more to the rest than they need to buy from them, while another is finding it very hard.

THE BRITISH DEFICIT

The British economy today is at an awkward corner in economic history. Already before 1914 her dominating position in world trade was beginning to slip. Two wars and the slump in between raised up rival local production in many markets. Lancashire now has to be defended against cheap textiles from countries whose indigenous industries she was once encouraged to ruin in the name of free trade. The other great staple export, coal, has been knocked out by technical developments. Rentier income—interest and profits on overseas investments built up in the era of trade surpluses and imperialist land grabbing—was an important substitute for exports. This was much reduced by the mobilization of foreign securities to pay for wartime supplies, and heavy debts were incurred (for wars also are conducted largely on market principles). Former privileges were lost with the dissolution of empire. The superior

efficiency of United States industry, not fully offset by higher wage rates, and the fast rise of Western Europe and Japan, has stiffened competition in export markets that England could once dominate without excessive exertion. On the other hand, the growth of population, continuous near-full employment and rising consumption increase demand for imports. High activity in a country without natural resources requires high imports of raw materials. Recently there has been a marked rise in manufactured imports also, for our modern rivals are competing with us, not only in third markets, but also at home.

It is natural enough that new competitors should raise their share in trade at the expense of an old one, but that does not make it any less painful. The failure of British industry to maintain its competitive position is partly due to complacency. The British business man thinks that British is best, and if the silly foreigners do not know it, that is their loss. This attitude shows itself both in lackadaisical salesmanship and in poor performance in design. It is partly due to the buoyant internal market, which makes profits easier to get at home, partly to reliance on traditional markets, which, as bad luck will have it, are those where income, and therefore demand, is growing relatively slowly and partly to an unfortunate choice in the industries to develop.

Rising costs have made matters worse, and relatively low prices would have helped to overcome other drawbacks, but it is vain to suppose that even a perfectly successful incomes policy by itself would do the trick.[g]

The tradition of laisser faire, that business men know best what is good for us, is sadly damaged by this experience, and its defenders now have to fall back on the argument of despair—that anything else would be worse.

But our troubles are not due only to the operation of the market system. A great contribution has been made to them by an inappropriate foreign policy.

Whether it was invented for that purpose or not, the

effect of the Cold War, in USA, has been to permit the 'military-industrial complex' to consume a great part of the fantastic productivity of American industry, thus keeping up prosperity and fending off depressions without having to resort to any means that challenge the principles of laisser faire. For the British economy it has been not helpful but disastrous. Expenditure on armaments absorbs as much as the whole of industrial investment in money terms[6] and takes a more than proportionate share of high technical skill and scientific ability. This has weakened our competitive power to an extent that cannot be estimated. (The flying start in post-war reconstruction both in Germany and Japan was much assisted by the prohibition on re-armament which compelled them to use their investable resources productively.) We have been obliged to lose the production of men kept under arms, and incur costs for keeping them overseas which throws a serious burden on to our balance of trade. The expenses of 'keeping the peace' by fighting little wars east of Suez used to be borne by India (the British balance of payments even profited from it when officers and administrators came home with their pensions). Now keeping up the show of strength when the substance has been lost weakens us still further.

Over and above all this, there is some aid to developing countries and a considerable balance of overseas investment by British firms in excess of foreign long term investment in this country. We need therefore a substantial surplus on the balance of trade to cover these outgoings, whereas actually we have a deficit. The balance meanwhile is covered by short-term borrowing, which gives rise to the financial problems discussed in the next chapter.[7]

STOP AND GO

Weakness in the balance of payments and slow growth of productivity set up a vicious spiral. To modernize industry there must be investment, but when investment is high activity is high. Imports are sucked in and the attraction of

the booming home market slackens the search for outlets for export. To counter a deterioration in the balance of trade, the traditional remedy is a credit squeeze. When the laisser faire system was run from London this mechanism appeared easy and smooth. The balance on *income account* (the balance of trade *plus* net income from foreign capital) was continuously favourable.[8] An overall deficit merely meant that the outflow of lending was excessive. A rise in Bank Rate was found to be sufficient to check it. On the basis of this experience the economists built up the myth of the power of monetary policy to control the economy. Bankers naturally like to believe in it for it asserts the authority of finance over industry. A check to borrowing, according to this theory, will curb demand, bring down prices, and 'restore equilibrium'.[h]

To act on the balance of trade (as opposed to the balance of lending) by monetary policy requires sufficient reduction in activity to cut imports—a brutal and wasteful remedy that cures the disease by killing the patient.

The strongest upholders of traditional ideas would not face actually carrying the policy through, but the periodic jerk to industrial growth each time it began to speed up was confusing and discouraging. No doubt this experience contributed to making the long-run problem worse. The panic of July 1966 pretended to be something different but in substance was pretty much in this tradition.

Slow growth, in turn, contributes to rising costs; a wages policy is much easier to carry out if the permitted average rise is say five per cent a year, than when it is two per cent. It allows more room for necessary relative adjustments to be made without raising the average too fast. Moreover a perceptible rise of real wages itself reduces dissatisfaction and so relieves pressure for more. Thus slow growth makes growth slower.

REMEDIES

It is clear enough that the old policy has come to a dead end. What other remedies are to be had? The best, of

course, would be a miraculous upsurge of zeal and energy in British industry, but the authorities do not seem able to find a spring to release it. Most people do not want to be strenuously efficient. They prefer to rub along, doing no worse than their neighbours, getting what enjoyment they can out of private life. This no doubt is a very sensible attitude to take. It is extremely tiresome, after winning the war, to be pushed around by defeated nations setting a pace of competition hotter than we care for.

Ambivalence

Whatever policy we do pursue we are sure to be complained of abroad. Our deficit is a scandal, upsetting the financial stability of the world in one way, but to remove the deficit, by whatever means, will upset it in another way, for, while it runs, the rest of the trading nations are benefiting from it. The capitalist world is normally a *buyer's market* in the sense that there is capacity to produce more than can be sold at a satisfactory price. Any one country that is buying more than it sells is helping to maintain profits and employment for the rest. To cut down the British deficit means to cut down the surplus of the rest, and whatever means is found to do it, the result cannot but be painful for them.

This introduces a kind of ambivalence into British policy. We are bound to offend, yet we cannot afford to lose friends. The objection to any measures that are proposed is precisely that they might do some good.

For instance, in 1964, a surcharge of fifteen per cent on manufactured imports was imposed. This was not intended permanently to redress the trade balance. It was a crisis measure intended to cause a sharp temporary fall in imports. Before it had had time to have much effect, complaints from abroad led to its reduction to ten per cent and it was announced that it would be removed in the autumn of 1966 (by which time a worse crisis had blown up).

Protection

The surcharge, in fact, was a breach of our engagements, In the era of reconstruction after the last war, one more attempt was made to restore the laisser-faire rules of the game, though with some modifications. The General Agreement on Tariffs and Trade outlawed various methods of subsidizing exports; it aimed at a general reduction of protective import duties and meanwhile prohibited any increase in preferences designed to steer trade into particular channels, except for the hundred per cent preference of a customs union, which the theology of free trade illogically allows to be acceptable.[9]

In any case protection cannot offer a permanent solution for the British problem. Protection in the short run helps the balance of trade by checking imports and steering demand to home goods, though dearer and less desirable than foreign alternatives, but, for this very reason, it takes off the pressure of competition from home industries and makes the long-run situation all the worse. On the other hand, to press ahead with GATT and secure an all-round reduction of tariffs would not solve the problem either, for our failure to export enough is by no means only due to the tariffs of other nations.

Devaluation

Another element in the post-war reconstruction was the institution of the International Monetary Fund, based upon the principle that exchange depreciation should not be permitted except to deal with a 'fundamental disequilibrium' in the balance of payments. If ever there was a case of fundamental disequilibrium, it is the case of Britain today, but a devaluation of sterling is by no means acceptable to the world financial authorities. No major country has autonomous control over its exchange rate. It can only depreciate if others are willing to be appreciated. At some stage no doubt a general realignment of exchange rates will have to be made. Meanwhile if we were free to suit

ourselves, a devaluation of sterling would be helpful, but far from a reliable cure.

Devaluation works by making all foreign goods dearer at home and home goods cheaper abroad. Thus it offers a general protection against imports and gives exports a competitive advantage. By the same token, it makes exports, and home goods rival to imports, relatively profitable to produce. In a situation where there is some unemployment and unused capacity in many lines, a devaluation increases activity and improves the balance of trade at one stroke. But when there is near-full employment already it is liable merely to increase the pressure of demand for labour, while the rise in price of imports increases the pressure for higher money-wage rates, so that before long the competitive advantage of lower home costs is completely lost.[10]

In short, so long as we slop along with near-full employment and laisser faire in all other respects, there is no way out of the wood.

Customs Union

The policy of joining the six nations who arrogate to themselves the name of Europe has been recommended as a solution for our problems. When the Common Market was first being discussed, the British scorned it. To compensate, the Free Trade Area was proposed, thus, as the wits remarked, setting Europe at sixes and sevens.[11] When the Six were seen to be more successful than ourselves, and their competition began to bite more painfully, we offered to join on terms of our own and were refused admittance. In 1966 ambivalence reigns.

Much wider issues are involved than questions of trade. In this country there is great objection to any sacrifice of national sovereignty and resentment at the prospect of damaging Commonwealth interests to please new partners. The Prime Minister has declared that Britain has the 'political will' to join, but the issue has not been put to the electorate, and opinion is evidently deeply divided. On the

other side, equally deep divisions exist, connected in particular with the relations between the United States and West Germany.

As far as mere trade is concerned, there does not seem to be any motive for the EEC to enlarge itself. The advantage of a customs union lies in countries offering each other a market, giving preference to imports from members in exchange for a preference in return, so that industries of each can specialize, develop productive capacity with a secure outlet, and gain the advantage of economies of scale. The preferences are given at the expense of outsiders. The wider the union, the less the advantage that it offers compared to the changes and chances of free trade.

From our point of view, there is no presumption, rather the reverse, that the gain to our exports from freer access to markets in the EEC would offset the increase of imports due to their access to ours. Suppose that our deficit grew, instead of declining, after joining the Six? Each of them has its own mixture of control with laisser faire, in many ways much more successful than our own,[12] but in relations between them the market rules of the game are strictly imposed. When full employment cannot be achieved with balanced trade, it is full employment that has to give way. Italy was recently subjected to this treatment[13] and there is no reason to suppose that we should be spared.

OTHER'S TROUBLES

An exceptionally large unbalance in international trade has been created by the violent swing of history that swept away the dominating position of Britain in the world economy, leaving unchanged the institutions and attitudes that belonged to it. But every country is liable to run into trouble at one time or another.

Just now the United States is suffering from a deficit of a very different kind from ours. Her favourable balance on income account is very large, but not large enough to match the outflow of government overseas expenditure and

of private capital seeking profitable investments abroad.[14] Fast growth, for instance in Italy and Japan, has to be curbed when imports run ahead of exports. France has several times escaped by means of devaluation.

It is even possible, though rare, for a country to have *too* favourable a balance of trade. The kaleidescope of competition may bring up a surplus of exports for a country whose government has no overseas obligations and whose capitalists have no particular desire to lend abroad. The balance is paid for by the rest of the world losing monetary reserves to the surplus country. According to the old orthodoxy, this should lead to easy credit and a stimulus to investment. But if there is already near-full employment the only consequence would be inflation. Investment at home could increase only if employment in the export industries was reduced. A situation of this kind, in Germany, has led to one of the very rare examples of an exchange rate being deliberately appreciated in order to reduce the competitive advantage of one country that was distressing the rest of the world.[15]

HAPPIER DAYS

How was it that the laisser-faire system seemed to work smoothly before 1914, without causing these continual embarrassments?

There were three main reasons. First, there was one principal source both of exports and of finance for the geographical expansion of capitalism. Investments were made in the New World or in colonial territories, where local industry could not provide the capital goods, and local incomes could not provide the saving. Investments, therefore, generated a surplus of imports, calling forth exports which came mainly from Great Britain. At the same time local institutions could not provide finance, so that overseas lending was called forth, which largely came from the same source. Thus there was a more or less harmonious development in the patterns of surpluses and

deficits on income account and of lending and borrowing, thrown up by untrammelled operation of the market system. The monetary mechanism had only to regulate minor discrepancies. When the mechanism was restored, in the Twenties, without the underlying harmony, it broke its teeth. The problems that it has to deal with in the Sixties are still more indigestible.

Second, British overseas investments were made, guided by the search for profit, mainly to open up sources of supply of food and raw materials for which a market was already in sight at home. Thus the investments were developing a flow of exports to match the interest and profits claimed by the capital that financed them.

Finally, no one in those days was bothering about employment. For the surplus country, when a fall in exports caused a slump at home, it was just too bad. So long as sterling remained strong, no action was required. In a deficit country which could not continue to attract profit-seeking loans, income had to fall till the deficit was eliminated. Deficit countries which were free to manage their own affairs resorted to protection to set up import-saving industries at home, and those which were not free remained 'underdeveloped'.

These were the good old days for us. But the smooth appearance of the system, when viewed from London, was partly an illusion. Under the surface, tensions were building up which presently broke it to pieces. It is foolish to feel nostalgia for a past that was all the time running on to produce the present.

III

INTERNATIONAL FINANCE

The problems of trade and capital movements between each country and the rest break surface from time to time in the form of a financial crisis.

Even in the heyday of laisser faire the national currency was admitted to be a proper concern of governments; since the national authorities were concerned about the currency, they had to be concerned about the balance of payments.

MEANING OF MONEY

Money is whatever is acceptable as a means of payment. Within one country some medium, such as treasury notes, can be constituted as legal tender, but there is no way of making the currency of one country acceptable in another merely by decree.

Official legal-tender money is supplemented, within each country, by credit. A claim upon a reputable institution such as a bank is acceptable by a third party. From this develops the convenient habit of holding deposits in a bank, transferable by cheque. The bank must keep a reserve of legal tender (partly in the form of a deposit with the national central bank) to meet any possible excess, day by day, of claims upon it over payments coming in; to maintain a good reputation its reserve ratio has to be seen to be ample. When a suspicion gets about that a bank might not be able to meet all the claims upon it, there is a *run*, each depositor hoping to get his money out before the others.

Nowadays, banks are hedged round with legal and conventional rules, in each country, precisely to prevent them from getting into such a situation, but the international credit system is still in a primitive stage of development.

International Reserves

For any one country the great bulk of in and out payments with the rest of the world as a whole cancel each other in the ordinary way, leaving from day to day a small balance on either side. Mutual convertibility of currencies, so that an excess of receipts from one can be set off against a deficit from another, is a great convenience to all concerned. An internationally acceptable medium of exchange is then required to settle differences between in and out payments of each country with the rest of the world. The duty of preserving the convertibility of its own currency falls upon the central bank of each country (in USA the Federal Reserve Board). Each central bank, therefore, has to hold a reserve of international currency, in somewhat the same way as an ordinary bank has to hold a reserve of national currency.

By a long historical tradition gold has become established as an internationally acceptable means of payment. There is a mysterious aura about it that makes it the symbol and embodyment of *value*, but as things are nowadays its value, that is its purchasing power over everything else, depends upon the price in terms of their own currencies that central banks will pay for it and the purchasing power over other things of those currencies.

Since 1933 the price of gold in terms of dollars has not changed, while everything else has risen in price. The value of gold in terms of everything else has therefore fallen. Moreover, the real value of the flow of trade and capital movements has grown and the number of countries taking part in the system has grown too.[16] For this very reason a system has developed of supplementing gold by claims upon an acceptable currency.[17] The dollar is an acceptable currency because of the dominant place of the United States in the capitalist world today, and sterling is acceptable because of a hangover from the dominant place it used to hold in the past and because of the great sophistication of the facilities for dealing in money that were then

developed in London. A balance in a respectable currency, so long as there is confidence in its convertibility and no fear that it will be used for political purposes, is superior to gold since it can earn interest, and can be passed around, when it has to be drawn upon, at much less cost. Not only central banks but all kinds of financial institutions find it convenient to hold balances in one or other of these *key currencies*.

Competition for reserves

This system is by no means satisfactory. At the present time both the key currencies, for different reasons, are suffering from a tendency to develop deficits and lose reserves. The traditional reaction of the monetary authority to a loss of reserves is to raise interest rates so as to make its currency more attractive. In so far as it succeeds in attracting deposits from foreign financiers, who now find it a more eligible place to hold their balances, it is offsetting its deficit on account of trade and long-term lending by short-term borrowing. This checks the outflow of reserves. So far so good. But it has solved its own problem largely by attracting balances away from other currencies, and so weakening them. Their authorities in turn have to raise interest rates to defend *their* reserves. The rise in interest rates and the credit squeeze required to make it effective set a drag upon investment in each country. Fortunately it has not so far succeeded in precipitating a world slump but it is pushing in that direction.

Before 1914

This deflationary twist in the international monetary system was not felt in this country when the gold standard was operated from London, because of the great strength of sterling. In a world boom, when investment was high, if lending ran ahead of the surplus on income account, a small rise in Bank Rate was sufficient to pull it back. The check to inflation was felt in the borrowing countries, not

here. Where world investment was low, lending fell off (for lack of borrowers) faster than the surplus of exports was reduced (by lack of buyers) so that sterling was strong. Unemployment due to the fall of exports did not have to be exacerbated by a credit squeeze at home.

1925-31

When the gold standard was restored, in 1925, sterling was weak, partly because of a greatly reduced surplus on income account, in the aftermath of the 1914-18 war, and partly because a rate of exchange with the dollar that was high in relation to relative costs was adopted under the influence of sentimental notions of prestige.[i] We had then been landed with the need for credit restriction when there was already unemployment. From this self-torment we were rescued by a crisis of confidence in sterling in 1931 which ran us out of reserves and so enforced depreciation of sterling. Meanwhile the capitalist world had plunged into the great slump; unemployment went on growing, but here the devaluation helped to brake it somewhat.[j] In 1933 Roosevelt devalued the dollar, by raising the dollar price of gold, not because the reserves were not ample, but because he thought it might help to relieve the slump at home.

A crisis of confidence

After the experiences of the Thirties, perfect confidence in the exchange value of any currency cannot be restored. When there is reason to expect that a currency might be devalued, there is a *flight*, similar to the run on a bank whose depositors fear it may be going to close its doors, everyone wanting to get their balances out of the weak currency and into a strong one before the devaluation occurs. The weakness of sterling, due to its persistent tendency to fall into a deficit on income account, combined with its position as a key currency holding large and volatile deposits, makes it chronically vulnerable.

Flights may also be set going for political reasons. An 'opening to the left' in one country meets with disapproval of financiers at home and abroad that expresses itself in a preference for other currencies. The position of a Labour government committed to maintaining the exchange value of sterling is peculiarly awkward, for it has to persuade its supporters that it is more radical than the Conservatives while persuading the international financiers that it is even less so.

The financial crisis arises out of the real problem of the balance of trade but it is something extra. It has, so to speak, a life of its own. It was, perhaps, possible to argue in 1964 than a devaluation of sterling would not by itself produce an adequate surplus of exports and that if the other measures required were taken it would not be necessary. On this view the policy of 'saving the pound' was justified so far as the real problem is concerned (though no doubt the decision was taken from political rather than economic motives). But, granting for the sake of argument that that view was correct, it is obvious that the repressive measures necessary to attempt to carry out the policy in face of a crisis of confidence makes all our problems so much the harder to solve.

International Liquidity

One way of increasing the supply of international money would be to raise the price of gold. This could be done between one day and the next by the Federal Reserve Board raising the price in terms of dollars that it pays for gold presented to it. Other currencies would follow suit. (Some might take advantage of the opportunity to raise their price a bit more, thus devaluing against the dollar and getting a competitive advantage against the United States.)

This policy has been persuasively advocated,[k] but it has serious drawbacks. The benefit of the rise in reserves would be arbitrarily distributed amongst central banks. The two

main gold producers, South Africa and USSR, who are not particularly popular in the capitalist world, would benefit from an arbitrary rise in the purchasing power of their exports. Above all, the prestige of gold would be so much raised and the prestige of the key currencies so completely shattered, that over the long run the available supply of acceptable international money would be reduced rather than increased.

A more rational expedient was proposed by Keynes when the post-war reconstruction of the world economy was being discussed.[1] He advocated setting up what was in effect a super-central bank, which would accept an agreed amount of deposits from national central banks, that could then be drawn upon in terms of a super-reserve currency which he proposed to name *bancor*. Bancor would have to be hedged around with safeguards to ensure its acceptability. Once acceptability as international money was established, it would constitute synthetic gold given out in the first instance in agreed quantities on some acceptable principle. and capable of being increased as the needs of the world financial community required. This scheme was rejected, under American influence, in favour of the International Monetary Fund, which only provides national governments with rights to borrow on somewhat onerous terms. The present highly unsatisfactory situation has set a current of opinion running in favour of some kind of bancor,[m] though it is always very difficult for sovereign nations to agree upon any kind of sensible scheme.

Sterling

The special difficulty of sterling is something over and above the general problem of international liquidity. A situation where, for historical reasons, a great mass of short-term liabilities is held in a currency which is blatantly and obviously subject to risk of devaluation, necessarily gives rise to flights or threats of flights from time to time. To maintain sterling as a key currency the international

financial authorities should have provided such large reserves as to appear convincingly ample to depositors, so as to maintain confidence. The measures necessary to restore the balance of trade could then have been undertaken without the added nuisance of a financial crisis. But that is not the sort of thing that international financial authorities do (partly because they believe that necessary measures never are undertaken without financial pressure). They patch up the situation with loans after a crisis of confidence has developed. Consequently the loans have to be drawn upon; the need to repay them is an added burden to the future balance of payments, and so the last state is worse than the first.

CAPITAL MOVEMENTS

The case of sterling in 1964 is only a particularly dramatic illustration of the fact that in the system of international financial relations now in force there are no generally accepted principles governing the exchange rates between national currencies.

The gold standard

The gold standard which broke up in 1914 had developed by a historical process without being consciously planned to work as it did. The monetary authority of each major financial centre undertook to buy and sell gold at a fixed price in its own currency. The price for gold which each chose fixed the rates of exchange between them within narrow limits. Convertability with gold was the ark of the covenant; the maintenance of the exchange rate was the dominant aim of all economic policy.

The rules of the game established under the gold standard ensured that no country could lend on balance to the rest more than its surplus on income account. When it did so, the offer of its currency on the exchanges exceeded the demand, the exchange rate fell below the gold parity, so that it became profitable to export gold. The consequent

drain on the gold reserve had to be stopped. By the same token no country could run a deficit on income account in excess of the inflow of capital that it was able to attract.

The other way round, it was possible for a country to lend less than its surplus on income account and so attract gold from the others, but this was not playing the game according to the rules. Its proper course was to reduce interest rates, which was intended both to increase its outflow of capital and to boost home demand so as to reduce its surplus.

British lending

The old gold-standard rule that a country cannot have a capital outflow greater than its surplus on income account is no longer in force. Great Britain is still carrying out overseas investment in spite of a deficit on income account. This adds to the weakness of sterling and has to be offset by short-term borrowing. Net purchase of foreign securities outside the sterling area[18] by British citizens is not allowed. The long-term lending is mainly in the form of direct investment in overseas enterprises and retention of profits earned on the spot.

From the point of view of the British balance of payments, it is defended on the ground that it will yield a future benefit, both in the form of remittances of profits and in the form of orders for suppliers of equipment and so forth which would otherwise go to rival exporters, so that prospective relief in the future justifies the extra strain in the present.[19] The cogency of this argument depends upon what other measures are available to redress the balance.

The aid being given to developing countries (a miserable trickle compared to all the talk about it) is mainly tied, to be spent only on British goods. In so far as it catches exports that would not otherwise be made, it is no burden on the balance of payments.

US lending

The capital outflow from the United States is partly in the form of purchases of securities representing capital that already exists. Owners of wealth in USA happen to find some foreign securities attractive. The payment of interest or dividends on these securities is then a future burden on the balance of payments of the country that sold them and will require a corresponding surplus on its balance of trade.

Besides this, the outflow of private capital from USA is financing investment, largely in the form of subsidiary branches of the great American corporations. This is no longer mainly of the colonial type, developing resources which will set up a flow of exports to match the profits that have to be paid to US shareholders. It is now largely directed to taking advantage of the market in a developed country.[20] Indeed, the subsidiary companies foster imports more than exports, for they set up a demand for spare parts etc. from their parent companies and give rise to remittances from expatriate staff. If Marx were right that capital seeks labour to exploit, the overpopulated countries of Asia, Africa and Latin America would be developing fast. Nowadays capital seeks a market for its products and provides itself with robots to substitute for labour. The local capitalists, with whom they compete, and governments fearing loss of independence, resent the system which allows this to go on.

A country, such as France, which has no deficit on income account but is yet receiving foreign capital in this way, matches the long-term borrowing that is taking place by short-term lending, that is, by acquiring dollar balances. General de Gaulle, regarding this is a swindle, demands payment in gold. This is one element in the weakness of the dollar. To defend the dollar, interest rates are forced up, and sterling catches a side blow.

EXCHANGE RATES

The second rule of the gold standard game was that any country where costs rose relatively to others, or which for

any reason lost ground in international competition, should suffer sufficient unemployment to bring its costs down. Convertability was sacrosanct; everything else must give way to it. It was this rule that proved unplayable in the great slump and caused the gold standard, partially restored in the Twenties, to break down in the Thirties.

Adjustable peg

The concept underlying the foundation of the International Monetary Fund was that currencies would be maintained (within certain limits) at the exchange rates ruling when it was set up, and that permission to change a rate would be granted by the Fund only in case of 'fundamental disequilibrium'. This concept is exceedingly vague. No attempt was made to define the criteria by which it should be judged. In any case the system was put afloat too soon in the choppy waters of post-war reconstruction and faith in the authority of the IMF was not established. Now exchange rates are the sport of national and international political pressures, with the unsatisfactory results that we see.

Floating rates

In the absence of any acceptable principles governing exchange rates, there is a school of thought which maintains that they should be left free for the market to settle.

When it is put in terms of the balance of trade, the argument sounds very attractive. Let each country maintain full employment. If it is not exporting enough to pay for the imports it then draws in, let the exchange rate fall, stimulating exports and restricting imports (provided, of course, that the benefit is not too quickly offset by a faster rise in money-wage rates) till balance is restored.

Admittedly, if the market were really free, violent and unhelpful perturbations would occur. To prevent this, central banks would have to maintain day to day stability in the exchanges, temporarily losing or gaining reserves,

while allowing movements appropriate to the competitive position of each country in trade.

What this means, in effect, is not that exchange rates would be settled by the market, but by the good sense and mutual helpfulness of central bankers finding the pattern of exchange rates that puts each country's balance right.

This would be all very well if payments for imports and exports of goods and services were the only transactions giving rise to demand and supply for foreign currency. But even if speculative movements could somehow be neutralized, long-term capital movements remain. In recent times, the dollar has been weak because capital outflows exceed an enormous surplus on an income account. Under the free market system, this would lead to a depreciation of the dollar, intended to make the surplus still greater. Other nations, faced with a growing deficit in trade, would have to depreciate in turn. The only result would be a general scramble to see who could get down lowest. If there is no right pattern of exchange rates that suits everyone, the central bankers cannot find it out.

The clash of national interests with international laisser faire produces a system of exchange rates that cannot be defended on philosophical principles. We have to live with it all the same.

IV

EMPLOYMENT AND GROWTH

WHATEVER may be the difficulties and confusions of partial laisser faire, it is greatly to be preferred to total laisser faire. In 1918 we were looking back with nostalgia to a pre-war world of prosperity and progress. In 1945 we were looking back to the fetid misery of continuous unemployment. Wartime experience of super-full employment had taught the people that the pre-war breakdown of the system was not inevitable and Keynes had produced a diagnosis of how it came about. A cure for unemployment after the war was the most insistent demand of democracy, and successive governments have met it pretty well.[21]

NEAR-FULL EMPLOYMENT

We should not be complacent. The persistence of unemployment in Scotland and still more in Northern Ireland is a serious blemish.[22] There has been some attempt to provide schemes for training workers for the skills that are in demand, schemes to soften the shock when a firm reduces its labour force, schemes to control the geographical development of industry to fit with the provision of housing; schemes to help married women to combine work for wages with work in the home, but they are in a rudimentary state. There is a great deal, in detail, that still needs to be done. But, by and large, the duty which governments now accept, of maintaining a 'high and stable level of employment' has been fairly well fulfilled.

The future is by no means secure. We have not yet seen whether the rest of the capitalist world could weather a serious recession in the United States; we cannot foresee how the trading nations in general and this country in particular will muddle themselves out of the international monetary

system they have muddled themselves into. But there is good reason to hope that nothing quite so stupid as the great slump will be allowed to occur.

In spite of the nuisance of rising prices, there are many incidental advantages of a high demand for labour, besides the main point—the avoidance of waste and misery. Management has to become more humane. Seasonal and casual trades are pushed into regulating themselves so as to be able to offer steady work. Dirty, ineligible jobs are cleaned up and made respectable. Firms which see a profitable market in prospect but cannot get hands have a strong motive to mechanize production, and the traditional fear of the workers that machines take the bread out of a man's mouth is reduced, if not yet fully overcome.

All this is very much to the good. Yet pursuing full employment as an end in itself is precisely what has landed the British economy in its present difficulties.

Functional Finance

The post-war orthodoxy was based upon a simplified version of Keynes' General Theory. In a market economy, the amount of employment offered depends upon the total money outlay, or *effective demand*. Demand is generated by expenditure for consumption; investment in the creation of capital equipment, buildings and stocks of materials and commodities; government outlay; and the production of exports. Expenditure for consumption depends upon income net of taxation; expenditure upon imports absorbs outlay without generating demand at home. According to the post-war orthodoxy, given the surplus or deficit in the balance of trade and the amount of investment which profit-seeking firms want to carry out, the government should regulate the overall level of effective demand through the budget. A deficiency of effective demand, leading to unemployment and under-utilization of productive capacity indicates that an increase in government outlay is required, or a reduction of taxation permitting an

increase in consumption. To supplement budgetary policy, the balance of trade can be influenced by commercial policy, and investment by credit policy.

It was quite alien to this point of view to consider that a surplus of exports, investment to modernize industry, government outlay for many purposes and consumption by the populace are all desirable uses for the nation's resources, or to inquire how the allocation between them ought to be made. Only the global total was considered to be proper object of policy.[23]

Employment policy since the war has been carried out more or less on these lines, reducing taxation when demand seemed to be flagging and squeezing credit when it seemed to be rising too fast. The aim of policy was to maintain the overall level of employment, without paying attention to what employment should be for.

Work for what?

Once the idea of employment policy has been accepted, full employment is no longer a rational aim. A rational policy would be to consider what the resources of the economy had best be used for, to work out a consistent plan, and steer them into the appropriate channels. This does not require the regimentation of labour. Even in the war, direction of labour, in the civilian sector, was very little used. Control operated upon the jobs that employers could offer.

The regime of near-full employment without planned use of resources came into being through a process of democratic competition. The Labour Party twitted the Conservatives with being incapable of preventing unemployment. The Conservatives twitted Labour with being devoted to austerity and regimentation. A Labour government carried out a bonfire of controls. Conservatives expelled from their ranks the advocates of sound finance. The choice of what employment should be for was left to the market to decide (apart from some public investment and expansion of social services) and the old laisser-faire

doctrine, that what is most profitable is best, reasserted its sway.

There are many grounds—moral, aesthetic, and political—for objecting to this system, on which opinions may differ; there is one about which it is impossible to disagree. Under the cover of easy profits and rising consumption, the balance of trade was allowed to drift until it has become clear to all that something must be done about it.

Defective Steering Gear

When near-full employment already obtains, it is not easy to shift its direction with only the instruments of policy which the new orthodoxy permits.

An increase in investment, without a reduction in consumption, merely adds to inflationary pressure. But if consumption is cut to make way for investment, profitability is reduced and the motive for investment impaired.

To increase exports immediately it is necessary to deflect goods which are saleable abroad away from the home market[24] and to make it easy for those firms which could increase the production for export to get labour. In the long run it is necessary to deflect investment and the recruitment of skilled workers and technicians into export industries. Resources have to be got *out* of the home market, as well as *into* the export market. Similarly if imports are cut down, the money that would have been spent upon them is deflected into the home market. Measures to boost the balance of trade have to be backed up by measures to reduce expenditure at home. But any overall measure such as a credit squeeze, a cut in government outlay or a stiff budget, is a blow with a blunt instrument. It is bound to lose much valuable activity that makes no contribution to the main problem. The wastefulness of an overall deflation of demand is not measured only by the unemployment of men who have been pushed out of one job and not pulled into another. There is also much useless sacrifice of output through short-time and slack working, and, worst of all, discouragement to investment and innovation, blocking the only hope of long-run improvement.

Redeployment

When manufacturing and service industries have grown accustomed to near-full employment, a drop in demand that appears likely to be temporary, is more often met by short-time working than by dismissing labour. There is a general tendency to treat more and more of the labour force as permanent employees, like the staff. From a long-run point of view it is highly desirable to make industrial relations more civilized. From a short-run point of view, *hoarding labour* is an impediment to movements of workers between occupations that would help to get economic activity into better shape. This reinforces the contention that overall indiscriminate deflation will not bring about the redeployment of the labour force that the situation requires.

The new device of a selective employment tax, intended to reduce recruitment of men into services so as to make them available for industry, is a step in the direction of discrimination but the discrimination is extremely crude.

One way Out

There is one kind of import that we could cut down without increasing inflationary pressure in the home market; that is, delusions of grandeur. To reduce military commitments overseas would bring a direct relief to the balance of payments while at the same time releasing manpower and other rescources for productive use.

ECONOMIC GROWTH

Once near-full employment has been achieved *growth* becomes the criterion of economic success. Growth is measured by an index of overall national product valued at constant prices. Since the division of national income between work and property is fairly constant, a high rate

of growth of national income means a high rate of growth in real wages.

Ever since the war the capitalist nations in general have felt themselves challenged by the spectacle of much more rapid growth in the socialist world, with which only Japan could compete. Amongst themselves, the performance of the United States and Britain has been markedly behind Western Europe. The absolute level of productivity in the United States is so much higher than in the rest, that they need not worry (they have plenty of other things to worry about) but Britain has been deeply chagrined by seeing the statistical measure of real wages in France and Germany surpassing hers and in Italy creeping up towards it.

Productivity

The chief engine of economic growth in a market economy (given the available labour force) is the application of technical improvements to production which comes about through the competitive struggle of firms seeking profitable outlets for investment.

The growth in the capitalist sector of the world since the war is a very remarkable phenomenon. Even in British industry productivity has been growing much faster than ever it did in the great age of her economic supremacy.[25] The system seems to have taken another lease of life and has adapted itself to exploiting the ever growing opportunities of applying scientific technology to production, though it has not yet shown whether it is capable of doing so in conditions of assured peace.

The virtuous spiral

Within the capitalist world, relatively rapid growth is a great advantage. It leaves room for money wages to rise without raising costs. It gives a competitive advantage in international trade and so allows home investment to boom without fear of provoking a financial crisis. Investment promotes productivity. Rising productivity improves the

country's competitive position, and so on round—the contrary of the vicious circle of slow growth and weak balance of trade which we know only too well.

Growth for what?

Yet, apart from the requirements of the balance of trade, growth for its own sake is not a rational objective of policy. It would be a rational use of growing resources to remove poverty, to clear up the hideous legacy of the industrial revolution, to build the schools and hospitals and train the personnel that the social services urgently require, as well as to modernize industry. It would be necessary to carry out technical and social research to see what needs to be done. The rate of return in benefit to society of investment would certainly be shown to be very high, so that such a policy would require growth for a long time to come. Growth should be the consequence, not the aim, of rational economic policy.

Distribution

To concentrate upon growth as the criterion of success distracts attention from the allocation of resources between public and private uses and from the distribution of income between families.[26] When growth is going on fast enough, all elements growing in proportion, the social services will grow, the lowest incomes will grow, the worst evils of poverty will be gradually overcome and so the demand for change in the philosophy and institutions of laisser faire can be fended off. Even with the low rate, by modern standards, of 2 per cent per annum, national income doubles within a generation. The ideology of growth is designed to prevent us from asking what we want to do with it.

The British Plan

The concept of growth as an end in itself is well exemplified in the so-called National Plan produced in 1965. This

was based on the idea that growth at the rate of 3.2 per cent per annum was practicable. Industries were asked to specify what outputs they could expect and what inputs they would need in a market growing at 4 per cent (allowing for .8 per cent growth of population), and the projections so obtained were then reconciled into a consistent scheme. The so-called planners did not feel called upon to suggest how the projection should be realized, still less whether it would be a good thing if it were.

Population

This argument concerns the growth of national income per head. Growth of population absorbs investment to provide social and industrial capital for growing numbers, and so reduces the rate of growth of income per head, not to mention the fall in amenities due to the reduction of space per head.

Immigration of workers similarly reduces the rate of growth per head, especially if they bring dependents with them, but it increases the growth of profit. So long as effective demand is kept up, additional workers make it possible to utilize existing equipment more fully, and provide an opportunity for investment in additional equipment without the need to seek out labour-saving methods, which may require an increase in investment per man employed and make profits harder to come by. Thus the objection of native workers to immigration, which takes the unpleasant form of xenophobia and colour prejudice, is justified by class interest. Meanwhile superstitions, rooted in chauvinism as well as religion, oppose the spread of facilities to prevent unwanted births.

V

MONOPOLY AND COMPETITION

ACCORDING to laisser-faire doctrine, competition between producers ensures that the best use is made of the economic resources of society to meet its economic needs. On this view, so long as competition prevails, there is no possible advantage from government interference with the free play of the market but distortions due to monopoly ought to be prevented.

FREE MARKETS

There is one sphere in which the market has free play, this is in dealing in certain animal, mineral and vegetable products which provide raw materials and food supplies for the wealthy industrialized nations. Demand for them varies with the general state of trade and with changes in tastes and techniques. Supplies vary with natural conditions such as droughts and plagues, with political events in the producing regions, and with the development of fresh sources of supply. The vagaries of supply and demand bring about violent movements in prices. If traders in these commodities could foresee what will happen next they would buy in and hold stocks when prices were abnormally low and unload when they were rising, thus making demand responsive to supply and supply responsive to demand. In turbulent conditions, however, foresight cannot be correct. Traders will often be buying on a rising market and selling on a falling market, exaggerating fluctuations instead of ironing them out.

Since, in the nature of the case, production of this sort is concentrated in particular regions, whole communities are dependent upon one or another commodity; the free play of competition therefore causes violent swings in their incomes. For this reason, the primary producers inside the

well-developed industrial countries are sheltered from competition by various schemes of regulation; the whole brunt of the market system is borne by the so-called developing countries, whose export earnings depend upon one commodity (or when they are lucky two or three) for which they were fostered as a source of supply in colonial days. The hazards of trade reduce their planning for development to a gamble and set them to cutting each others throats by competing for sales in a buyer's market.

The balance of power is with the manufacturers who import these materials, for when supplies are excessive they can enjoy low prices; when the market goes up, they recover from the public at home by adding the additional cost into their selling prices; when supplies of one kind of material are deficient they can usually switch over to using a substitute, which sometimes turns out to be even preferable once they have adapted their manufactures to it. For this reason they have put up a powerful resistance to various schemes that have been proposed to regulate trade in a manner that would limit their freedom to take advantage of the play of the market. But for the industrial nations as a whole this system has a serious drawback; the suppliers of raw materials are buyers of manufactures (including the investment goods required for development); violent fluctuations in the incomes of their customers cause fluctuations in the demand for their exports, which are a considerable nuisance, as well as giving rise to the reproach that all their fine talk about aiding development is mere hypocrisy.

The one case where free competition operates is not a very good example of its supposed benificence.

REGIONAL PROSPERITY

Where a particular industry, such as shipbuilding, subject to foreign competition, is concentrated in a particular region, the situation there is somewhat similar to that of a primary-producing country. The income of the region

fluctuates with the state of demand for a particular output. For this reason, a pre-condition for near-full employment was a policy for geographical development, aimed at getting a mixed bag of industries in each district, and promoting the location of growing industries side by side with those that are shrinking—for instance, engineering in Lancashire to make up for cotton. The policy has not been completely successful. There are backward regions in Great Britain as in all the advanced countries. The drift of population and of wealth to the South East is hard to check. But, by and large, there is a fairly uniform level of wages for comparable jobs, all over the country, and a fairly uniform level of profit on capital for comparable types of business. That is to say, that (unlike primary production) the incomes drawn from an industry are independent of the prices at which its output is sold. Prices are governed by costs instead of incomes being governed by prices.

IMPERFECT COMPETITION

The manner in which manufactured goods are sold is unlike the marketing of primary commodities. Instead of output, already produced, being thrown on the market and sold for what it will fetch, the manufacturer offers to sell, at a price which he choses, as much as the market will take.

Economists make a great deal of fuss about the theory of prices, but to a businessman it appears as though prices pretty well settle themselves; his preoccupation is with getting sales. 'Of course the price has got to be right' he will say. That is, he does not want to lose sales by setting a margin which will give his competitors an advantage; at the same time he does not want to lose potential profit by charging a lower price than that at which he expects to be able to sell a reasonable level of output. Thus the price that each charges depends very much upon what the others are doing.

A scoop

New commodities are put on the market at prices governed by those for which they are substitutes. When there has been a dramatic fall in costs, this may lead, for a time, to Himalayan profits—the first ball point was sold at the price of a high-class fountain pen.

Price Leadership

For established lines, the margin that one producer will choose is governed by the prices that others are charging for similar goods.

This naturally sets up a tendency to blunt the edge of competition. The mildest kind of collusive behaviour is the institution of *price leadership*. One firm is tacitly recognized by the rest as the bell wether. When its price goes up, they all go up. No one will cut price until it does. The firms compete through salesmanship of all kinds and through the design and packaging of their products, but eschew competing in price.

Restrictive Practices

Formal agreements are sometimes set up to take advantage of a strong demand for some new product. Margins are set high and the market shared out by agreement. The price is regulated by the level at which the highest-cost producers are viable; the low-cost producers limit output and enjoy high margins.

More often rings are formed as a defence against price cutting in a buyer's market. When demand has fallen so that it is impossible to sell normal capacity output at the pre-existing price, it suits the firms best to maintain the price and allow output to fall, for if one began to cut price, attempting to get a larger share of the market, the rest would have to follow, and they would all end up with not much more output and much lower margins.

In a deep slump, mere fellow feeling is not strong enough

to prevent price cutting and rings are formed in order to share the limited market so that all can survive.

Rings formed defensively persist after demand has revived and are used to enhance its profitability. They commonly resort to various devices to keep non-members off the grass—for instance making it worthwhile to retailers to refuse to handle their goods. They impede technical progress by resisting innovations, setting a drag on the growth of the more efficient producers inside the ring and strangling would-be competitors outside.

During the slump, public opinion and legal decisions rather favoured agreements that were seen to be primarily a defence against cut-throat competition. In the post-war era of seller's markets they are seen as grabbing an unwarranted share of profits for themselves and as impeding growth and progress.

Legislation against *restrictive practices* has had some success. It is not easy to make firms compete if they do not want to but it is possible to remove impediments from those who do want to compete.[27]

A notable example of this is the prohibition of *resale price maintenance*, under which all retailers were obliged to maintain the level of margins, on a wide-range of goods, that old-fashioned shops found satisfactory. This system was holding up the development of self-service stores, which is now roaring ahead.

Monopoly

The main count against rings and restrictive practices is that they prevent the more efficient firms from knocking on the less efficient as fast as they might. When competition is unrestrained and carried on with vigour, the size of firms grows and the number in any one industry falls. The logical end of competition is monopoly.

A large and powerful firm enjoys economies of scale. It can afford to carry on research. It can risk pioneering new methods of production and new commodities. It can pro-

vide good conditions of work, and is not averse to paying high wages which embarrass its weaker competitors.

On the other hand, since excess capacity is the thief of profit, it may prefer to keep investment in the rear of demand, and so ensure a certain degree of scarcity for its products. It may grow sluggish and suffer from bureaucratic hardening of the arteries. The dominating position in its markets that it won by superior efficiency may be defended by dirty tricks. Its research may turn from making discoveries of its own to frustrating the discoveries of others.

The benefits and the drawbacks to the economy of the existence of powerful monopolistic firms spring from the same source. Legislation cannot do much to secure the one without the other.

Part of the revulsion in favour of competition under post-war prosperity was the institution of a Monopolies Commission. Its task is to review cases where serious abuse of monopoly power is suspected. No doubt it has done some good in establishing a code of proper behaviour.

The drive against monopoly is regarded partly as a *quid pro quo* for wage restraint. It has no doubt contributed to the all round reduction in profit margins which has been experienced in recent years.

Oligopoly

The typical form of modern industry is neither competition nor monopoly but *oligopoly*—each market is dominated by a few large firms, surrounded by small fry who fill various niches—often very profitable—that are left vacant, in specialized production, bespoke work, distribution and so forth.

The process of competitive struggle, big fish eating the little ones, often comes to rest before the final emergence of a monopoly. Then two or three firms remain, each not daring to challenge the rest to the final round. They then continue to exist, each striving to maintain its share in the principal markets that they serve, largely by sales pressure

of various kinds,[28] and meanwhile nibbling away on the flanks, expanding into other markets still occupied by weak competitors.[n]

Oligopolistic competition occasionally takes the form of a price war in some particular range of products, but most of the time it is concentrated upon designing new varieties of commodities and methods of production. So long as the oligopolists keep each other on their toes this is the most progressive of all forms of industry (in spite of the wastes of non-price competition), but if they fall into a mood of live and let live they may become as sluggish as outright monopolists.

Robots

The mechanization of industry is continuously raising output per man hour, that is reducing the amount of work required to produce a unit of output. With automation this process has taken a great leap forward and is now invading clerical work at a rapid pace. This threatens to reduce the share of wages and increase the share of profits in the proceeds of industry. So far its effect has not been much felt, but it may well be creeping up upon us under cover of the present short-period scarcity of labour.

When output is not growing fast enough to provide an outlet for investment to absorb saving out of profits, an upward drift in the share of profit sets a drag on the growth of effective demand so that *technological unemployment* tends to emerge. In such a situation, to stimulate rentier consumption would help to maintain effective demand, but this is a remedy for unemployment scarcely more rational than the famous expedient of paying men to dig holes in the ground and fill them up again.

A more acceptable policy would be to require generous severance pay and to provide appropriate retraining schemes to increase *mobility of labour* without excessive hardship; to raise hourly wages and shorten the standard week or to increase holidays with pay, to shorten the standard

year, so as to permit the workers as a whole to take out their share of the potential increase of national income in the form of leisure; and to mop up the redundant saving out of profits by taxation to be spent on social services. It is not inevitable that growing productivity should be a cause of misery.[29]

GOVERNMENT BUSINESS

There are certain industries—for instance railways, electricity and gas—which, for efficiency of operation, have to have a monopoly in each district because they have to have a network of lines of supply. For this reason it has always been recognized, except by the most fanatical supporters of laisser faire, that they have to be controlled in the public interest. Since, moreover, a unified national network offers technical advantages, it is generally agreed that these services should be nationalized.

The coal industry was nationalized rather because it had got itself into a mess under private enterprise. The nationalization of steel is proposed on the ground that the basic investment industry ought to be controlled in the public interest.

The services provided by the government are the most important for comfort—compare the benefit of having electric light rather than oil lamps with the benefit derived from any other item in the household bills, apart from the necessities of life—and they are the most basic for production.

The nationalized industries are instructed to follow a price policy that covers costs, so that expansion has to take place through government borrowing. Private enterprise raises the greater part of the finance for its investments out of profits. (When you buy a packet of goods, over and above the cost of producing, advertising and selling it, you are generally paying a subscription to the expansion of the firm concerned.)

Public corporations are designed partly to defend the

consumer from the ill effects of commercialism—broadcasting to check the erosion of taste, and air lines the erosion of safety, by the pursuit of profit.

The medical and education services make the greatest contribution both to welfare of individuals and to providing industry with an adequate labour force. To correct the worst effects of inequality of income they have to be provided out of taxation.

There are other services which might well be provided in the same way, and we are constantly being promised positive action to set up public enterprises where private enterprise has neglected an opportunity to develop new technology or where an old established industry is suffering from hardening of the arteries;° the old slogans of laisser faire—that government outlay is more inflationary than private and government services less valuable to the nation than those that earn profits—are still often heard, but they carry less weight at a time when there is so much dissatisfaction about the slow growth of productivity in private industry in Britain and failure to keep abreast of its rivals in Europe.

CONSUMER'S SOVEREIGNTY

There is an enormous fall-out of benefit to the consumer from the competitive search for profit in private-enterprise industry. We owe to the search for ever new markets —to name only two examples—stylish ready-to-wear clothing, which has contributed to democracy by breaking down class distinctions; and the development of household gadgets, which first stepped into the vacuum in middle class families caused by the disappearance of domestic servants and are now beginning to lighten the toil of working-class wives.

All the same, it is absurd to maintain that the private enterprise system is directed towards supplying consumer's needs. Rather, consumers are the pasture on which enterprise feeds. We are used to a system that is run for the benefit of producers, in which the advantage to consumers

is merely incidental, and since each of us has a strong, concentrated interest in his position as an income-earner and a weak, diffused interest in his position as a consumer, the system is found to be generally acceptable. This tolerance is illustrated by certain characteristics of the system which are quite familiar but rarely rouse protest.

Take, for instance, the question of durability. There are many objects of daily use, untouched by fashion, in which resistance to wear and tear is a great benefit to the buyer. The producer, of course, prefers frequent replacement. The producer controls design and quality. Moreover it is to the producer's interest to speed up the wheel of fashion and spread its influence over ever wider fields, inducing *psychological obsolescence* of models already sold by making small improvements in new models or merely by changing appearances, so as to appear to the consumer's desire to show off to the Joneses.

A second example is the manner in which goods are sold. Manufacturers commonly compete with each other in the terms that they offer to retailers. The shopkeeper then ceases to be his customer's friend, offering the best possible selection of goods and the best advice. He is induced to push some products and refuses to offer others (which might suit the customer better) because they do not carry such a large margin for him.

The main example of this phenomenon, of course, is advertisement. In the sacred name of competition we have to allow the advertisers to debauch public taste with snobbery and vulgarization of sex. When they try to raise the tone with reproductions of old masters and quotations from Shakespeare, they are still more nauseating.

A case for advertisement is sometimes made out on the ground that it provides information about the commodities available in the market. If so, the information that it conveys is often erroneous—for instance that tigers are good at driving motor cars or that drinking stout promotes muscular development.

Specialist agencies carry out elaborate research, not to find out what the housewife needs, but to discover how she reacts to various types of salesmanship. A large part of advertisement is devoted to *creating wants* for useless or harmful merchandise, in order to supply them. The consumer would clearly be better off without the wants and without the supplies. Specialist journals to some extent provide genuine information and criticism of design in particular fields; *Which* is making a gallant attempt to perform the same service for the general market; the mass of consumers, however, are too much doped to pay attention.

This system of competition in salesmanship no doubt, is the best system we have got, but it is idle to pretend that it operates, as the text books claim, so as to produce the maximum satisfaction possible with given economic resources.

VI

WORK AND PROPERTY

KEYNES' description of capitalists who 'were allowed to call the best part of the cake theirs . . . on the tacit underlying condition that they consumed very little of it' applied to the old-style entrepreneur managing a business that he had built up from his own resources. There are still sometimes great fortunes acquired by individual tycoons and there are still family businesses which have not yet become public companies or been absorbed into one of the great amalgamations. In the main, industry and trade are now dominated by *managerial capitalism*, that is by companies nominally owned by a shifting population of shareholders and actually run by salaried staff.

RENTIER INCOME

The principle of limited liability enabled managerial capitalism to grow up over the last hundred years. An owner of wealth can spread his risks by holding shares in many companies about whose business he knows nothing except what may affect their value on the Stock Exchange. His rights as an owner of a company concern him only in cases of emergency. The return on shares, from his point of view, is merely an alternative to interest on a loan, and his role in business is simply that of a *rentier*, just as much as though his wealth were placed in gilt-edged government bonds or derived from rent of land.

Unearned income

Rentier property, as a social institution, provides a number of conveniences. It pays a premium on savings designed to carry purchasing power forward to a time when family needs will be greater. It provides for widows and

orphans in the middle class. It provides endowments for many worthy institutions. The returns which insurance companies and pension schemes get on their funds improve the terms that they can offer. For the most part, however, its function is only to provide what the Inland Revenue rightly describes as *unearned income* to the heirs of entrepreneurs and to contribute taxes to the exchequer, just as rent from land provides unearned income to the heirs of feudalism.

The Stock Exchange

Amongst possible placements from which rentier income can be derived, shares issued by limited liability companies of all kinds are particularly attractive, especially in a period of chronic inflation. But a share is a *share* in the fortunes of a company. In the hurly-burly of competition individual fortunes cannot be foreseen. Moreover taxation distorts relative yields in a complicated way, and the market as a whole is liable to swing up and down with changes in level of rates of interest (which, as we have seen, are connected with the international financial situation), with waves of sentiment and with the interpretation that it puts upon political events. Dealing in shares is by no means a simple matter. A great apparatus of jobbers, brokers, advisers and financiers has been created to assist the rentier in placing his wealth. The game of spotting winners then develops as a by-product that swallows up the original purpose for which the institution was created. This game is not easy and it can be lucrative. It therefore attracts a great deal of high-class brain power from more constructive activities.

Redundancy

The contribution which the capital market makes to providing finance for industry is very small in relation to the resources that go into keeping up the whole affair. The existence of the market facilitates raising finance by new issues, but this is a minor part of the finance which industry

absorbs, since the greater part is provided from retained profits.[30]

For its hierarchy of managers, a company takes on a life of its own, like a college or a regiment; their loyalty is to the company as such rather than to the shareholders. From their point of view the distribution of dividends is a necessary evil; the proper use for profits is investment to enlarge the operation of the company.

In this way we have drifted unconsciously into a highly peculiar economic system. The net earnings of a company belong to its shareholders. They receive them either in the form of dividends or in the form of the rise in the value of shares corresponding to the earning power of additional investments financed by retained profits. They are free to spend these capital gains for consumption. In so far as they do not spend them, the system so to speak credits them with saving. The wealth generated by technical progress, capital accumulation, work and business acumen, thus drop into the laps of rentiers while they sit at home or occupy themselves with other tasks.

The old excuse for the existence of a wealthy class—that they are necessary to provide savings—has worn extremely thin. On the contrary, it is their consumption which is a draft upon the nation's resources.

The excuse that the stock exchange provides a good guide to profitability and so channels finance to where it can best be used, was never convincing and it was laughed out of court by Keynes' description of the manner in which the market operators, like those who go in for a newspaper competition to select the most beautiful film star, make their gains by 'anticipating what average opinion expects average opinion to be'.[p]

OWNERSHIP AND CONTROL

To a certain extent, the divorce between ownership and control has softened the rigour of laisser-faire capitalism. The managers must pursue profits for their firm to survive

and grow, but good reputation and humane labour relations may also be their object. Equally, so may be an easy life and long weekends.

The freedom of managers is, however, circumscribed by the legal fiction that the shareholders own the company. The group of rentiers who, at any particular moment, hold the company's shares regard them merely as an eligible placement for a fraction of their private wealth. They see no objection to selling their holdings to anyone who offers favourable terms. Thus when, for good reasons or bad, the stock exchange value of a company falls below the potential profitability of its real assets, it is in danger of a *take-over bid* from another company or an individual tycoon who can buy up the business behind its own back, throw out the board of directors, prune the management and switch to a more profitable, though not necessarily a more admirable, line than was being pursued before.

The market (especially in England) values shares more by dividends than by earnings. Thus, to make itself less tempting for a take over by keeping up its *valuation ratio* (the stock exchange value of the shares over the value of the earning assets based on expected profitability) the management must pay out more dividends than they would like.[q]

THE NATION AS RENTIER

In spite of its drawbacks, managers generally value the freedom that this peculiar system gives them. For the most part, they dislike the idea of being nationalized or even of being financed by a public body which would have a right to supervise them. The great financial institutions such as insurance companies, which actually own a great deal of industry, lean backwards not to interfere. In principle, there is no reason why the state should not also enjoy ownership without control where management by private enterprise is considered preferable. A budget surplus *above the line*, that is on income account,[31] instead of being used

to check the growth of the national debt could be used to buy industrial shares.

In a period when there is continuous economic growth in real terms (cancelling out the falling value of money) through rising productivity, when land, labour and capital each receive fairly constant overall shares in net national income, the total of private property is growing, but the prospect of a long run rise in the value of any particular company is highly speculative so that it is heavily discounted in its present value. If, for the sake of argument, we suppose that a good lot were taken over, they could each be bought at market price, and the value of the lot would be certain to rise, giving a fair profit to the nation (not to mention the unfair profit due to inflation). Rentier consumption would be *pro tanto* stabilized, and its erstwhile growth could be devoted to public expenditure, public saving through a budget surplus, or reduction of taxes on earned income. This is not so much a programme as an illustration of the nature of rentier wealth.

The corresponding proposal to take over property in land has often been advocated. The longer it is put off, the greater the unearned increment of private wealth.

INHERITED WEALTH

The large fortunes built up during the process of accumulation that Keynes described, as well as those inherited from feudalism, have left a permanent legacy of great inequality of property. It perpetuates itself, for one finds it easy to make money if one has some, and next to impossible if one has not.

Progressive Taxation

Inequality is not accepted by the democratic conscience and has to be combated by taxation. The apparatus of taxation is expensive; whatever criteria of taxable capacity are devised are necessarily somewhat arbitrary and set up meaningless distortions in the values of different kinds of

property; a great deal of highly expert man-power is devoted to advising rentiers and businessmen on legal tax avoidance (not to mention the other kind); the legislative, administrative and legal apparatus of the country is burdened with the task of making the tax system fair, or appear fair, as between equal incomes, and the definition of income for tax purposes has developed an elaborate body of theology which is a constant source of dispute. In short, the whole affair is a great nuisance.

In spite of all, inequality remains. Progressive taxation has made scarcely a dent in it.[32]

Standards of life

Inequality in post-tax income and capital gains gives rise to inequalities in consumption which make it very hard to persuade the trade unions that incomes policy is on the level.

Families with high incomes cannot be prevented from spending them on what they most need, and so the two-tier system of health and education services is perpetuated, and contributes to perpetuating inequality.

A drastic remedy

The concept of the nation as rentier points the way out of this situation. Concentrations of private property could be wiped out in a generation by confiscatory death duties (leaving a reasonable life interest to widows and orphans, and buttressed by equally heavy taxation on gifts). The titles to property could be handed over in the form in which it exists, to be held like any other endowment of a trust, and the income from it devoted to public purposes. This would not merely check the growth of rentier income, as nationalization with compensation does, but take a large bite out of it.[33] In particular, the reduction of fee-paying demand would make it possible to unify and improve the health and educational services.

Salaries

There is another source of inequality also connected with the share of profit in the proceeds of industry—the high salaries and perquisites of business executives. They, even more than the pay of skilled workers, are subject to wage drift in the competition between firms for the best men. They subject education, research and the learned professions to a brain drain which has to be answered by setting up comparable salary scales—infecting the republic of letters with demoralizing commercialism.

This could be checked by the Inland Revenue refusing to allow, as costs for tax purposes, salaries above a certain multiple of the average wage. There would of course be a great outcry about *incentives*, but incentives are relative. 'The game can be played just as well for lower stakes once the players are used to them.'

Why not?

The obstacles to such schemes are neither technical nor legal. They lie in the political opposition that could be rallied against them at home and the threat of flights of capital and capitalists to more congenial shores. (In the Common Market they could not be attempted until the whole of Christian Democracy was converted to the idea.)

The main obstacle, all the same, to eliminating functionless wealth is lack of imagination in developing ideas and institutions appropriate to an economy that has got over the hump of heavy accumulation and needs to find a rational way of enjoying the benefit.

CONCLUSION

In the foregoing, the problems of partial laisser faire have been illustrated by reference to British experience. The reader, no doubt, is anxious to ask: What should be done? On this I can only offer my own opinion for whatever it is worth.

It seems to me that the people of this country are not in the mood for radical change. They prefer a loose-jointed, ramshackle economic system to one streamlined for efficiency and speed. They are willing to accept much that is irrational and unjust for the sake of preserving the continuity of our political institutions and the glorious flummery of Church and State.

But, at least the rising generation, resents privilege and snobbishness and demands genuine equality of opportunity for everyone to use what talents he may have. They are perfectly ready to shed the last rags of empire and settle down to being a small country devoted to neutrality and peace.

The transition to such a line of policy could not be quick and easy, but if the aim was clear, the way would be found. After all, we knew how to set up the machinery that was required to mobilize the economy for war. It could not be so hard to get a sufficient grip upon it to deal with our present misfortunes.

It will be objected that the war was a matter of life and death. Patriotism and enlightened self-interest combined to suspend privileges which would never be given up in peacetime. But the evident failure of laisser faire with near-full employment once more rallies enlightened self-interest to accept whatever is necessary to make the system work. Besides, the argument cuts both ways. The people responded to the call of blood, sweat and tears to save the country from destruction and to defeat Fascism.

They are not so ready to make sacrifices in order to support an ambivalent, vacillating policy that, pretending to maintain national greatness, is undermining its economic and moral basis.

While drawing upon the hump of resources locked up in military expenditure it would probably be necessary to curtail the overall growth of consumption for some time, to get the balance of trade in order and disentangle sterling from the international monetary system by paying off the short-term indebtedness which keeps it in thrall. Meanwhile we could overcome the worst poverty, and, once we were round the corner, we could set about to make a country where all can be comfortable, cheerful and free to follow their fancies.

This is a selfish ideal. Democracies are selfish. They think of the nation, not of the world. Two menaces hang over the world today—the rise of population ahead of economic development which is spreading desperate misery in the southern continents, and the American crusade against communism, which threatens worse horrors than it is already perpetrating and meanwhile prevents each economic system from settling into peaceful co-existence with the other and using its resources to meet its urgent needs. Compared to these, our problems are trivial, but until we have settled those little problems we are powerless to use any influence at all to contribute to the great ones.

NOTES

INTRODUCTION

[a] *Economic Consequences of the Peace*, pp. 16–17.

[1] I use laisser faire in a broad sense to mean the complex of ideas and policies that grew up with the 'remarkable system' that Keynes described. Its principle tenet was that the sole duty of government in economic affairs was to preserve the value of money at home and abroad by balancing the budget and maintaining convertibility of the currency with gold.

The expression has become naturalized; in what follows it is printed without italics.

1 INCOMES AND PRICES

[2] Total consumer's expenditure (including rent) reckoned at prices ruling in 1958 was £13,106 million in 1950 and £18,943 million in 1964, an increase of about 45 per cent. In this period, the resident population rose by about 8 per cent, so that there was an average increase in consumption per head, man, woman and child, of about 34 per cent.

(National Income and Expenditure, 1965 and *Statistical Abstract*, 1965).

[b] This view of the determination of prices is based on the theory first formulated by Michael Kalecki in *Essays in the Theory of Economic Fluctuation*, 1939. It has been supported by statistical observations in *Wages and Employment in the Trade Cycle* by R. R. Neild, 1963.

[c] See below, p. 53.

[3] In 1965 it appears that the prices of manufactures rose less than wages, while prices of materials were more or less constant, as follows:

	1958 = 100	
	1964	1965
Earnings per head	137·5	146·1
Price of manufactures	111·5	116·7

(National Institute of Economic and Social Research, *Economic Review*, May 1966.)

On the other hand, prices do not always fall with costs.

The Cohen Council in 1959 (see below note 5) was reporting on the aftermath of the first recession since the war that had raised unemployment to more than 2·5 per cent. Wages had risen very little over the preceding year and raw material prices had fallen. The Council deduced that for many industries costs must have fallen and strongly urged that prices should be cut. The spokesmen of industry, however, thought this a strange doctrine.

> There are ambiguities in its suggestion that industry should reduce prices. It is one thing to reduce prices and thereby expand demand and output; it is another to hold prices below their market level with the object of curbing profits or dividends.
> (A statement by the Federation of British Industries reported in *The Times*, August 7th 1959).

It is possible that since that date the industrialists have grown more sophisticated.

[4] The following appeared in *The Times*, January 23, 1943:

> Unemployment in a private-enterprise economy has not only the function of preserving discipline in industry, but also indirectly the function of preserving the value of money. If free wage-bargaining, as we have known it hitherto, is continued in conditions of full employment, there would be a constant upward pressure upon money wage-rates . . . In peace-time the vicious spiral of wages and prices might become chronic.
> (Joan Robinson, *Collected Economic Papers*, Vol. I, p. 85.)

[5] The White Paper of 1944 on *Employment Policy* (Cmd 6527) marked the official acceptance of the view that it was possible and necessary for government action to maintain a

'high and stable level of employment'. It was not until 1957 that doubts about the orthodox view of prices led to the appointment of the *Council on Prices, Productivity and Incomes* (the Cohen Council). Its first two reports, however, supported orthodoxy. The third, in 1959, when Professor Phelps Brown had succeeded Sir Dennis Robertson as the Council's economist, seeks to analyse the determination of prices in terms of costs and profit margins.

In the same year the Report of the Radcliffe Committee on the *Workings of the Monetary System* undermined belief in orthodoxy by showing how weak was the control of the authorities over the monetary system, and how uncertain the effects of monetary policy in the economy. In 1961 a National Economic Development Council, and a National Incomes Council (Neddy and Nicky), were set up. These were the first tentative and rudimentary attempts to produce new organs for economic planning in this country. They provide a symbol of official recognition of the end of laisser faire.

Neddy still survives, but is now overshadowed by the Department of Economic Affairs. Nicky was wound up by the Labour Government in 1964 and superseded by the Prices and Incomes Board.

[d] See J. C. R. Dow, *The Management of the British Economy 1945–60*, p. 403.

[e] See *U. N. World Economic Survey* 1964, Part II, p. 42. This section of the *Survey* gives an account of the general state of opinion on the question of incomes policy in the industrial nations.

[f] Cf. Barbara Wootton, *Social Foundations of Wage Policy*, especially chapter II, 'Some Economic Curiosities of the British Wage Structure.'

II THE BALANCE OF TRADE

[g] A summary and analysis of the various factors retarding British exports is given by M. Panic and T. Seward, The Problem of UK Exports, Oxford Institute of Statistics,

Bulletin, Vol. 28, No. 1, 1966. The behaviour of imports is described and the need for import-saving investment argued in 'Re-thinking Foreign Trade Policy,' by Austin Robinson (*Three Banks Review*, Dec. 1963.)

[6] In 1964 expenditure on armaments was £2,000 million, about 7 per cent of gross national product. In the same year gross private investment in plant, machinery and vehicles was £1,800 million. The whole of gross investment in fixed capital (including the purchase price of sites) was £5,800 million.

Expenditure on the health service was £1,100 million and on education £1,400 million.

(*National Income and Expenditure*, 1965)

[7] The categories, income account, long-term capital account and counterbalancing monetary movements, are not clear cut; each shades into the other at the edges. Different countries publish their accounts in different forms. For instance, the US Department of Commerce includes in monetary movements some items that in the UK accounts appear as capital. The treatment of re-investment on the spot of profits accruing abroad is partly included in the US outflow of capital, but not for the UK.

However, for purposes of the present discussion, we need only consider the broad headings. The income account is made up of receipts and payments for imports and exports (visible trade), receipts and payments for services for shipping, insurance, etc., and receipts and payments for interest and profits from overseas assets (the invisible items).

In the accounts, governments military expenditure overseas appears as an invisible import. In setting out the accounts here and in note 11 below this is shown as a separate item.

Long term capital account consists of purchases of foreign securities, private and government loans and direct investment in enterprises overseas.

The position of the UK balance of payments for 1964 as follows:

	£ million
Deficit on income account	−138
Overseas military expenditure	−274
Net capital outflow	−344
Errors and omissions	+ 35
Balance of monetary movements	721

(Errors and omissions is the balancing item which reconciles the records of the income account with records of monetary movements.) (*National Income and Expenditure*, 1965)

The increase in exports necessary to achieve balance if there were no cuts in outflows would be a little less than 3 per cent of gross nation product. Something more would be required to repay the credits used up during successive crises.

[8] See Phyllis Deane and W. A. Cole, *British Economic Growth, 1688–1959*, pp. 33–8 for a summary of history of the balance of payments. The surplus on income account was at its height in the decade before 1914. The balance dwindled after the war and turned negative in the thirties.

[h] The *locus classicus* for the economists' myth is the Cunliffe Report of 1918. See 'A Note on Bank Rate,' Joan Robinson, *Collected Economic Papers*, Vol. II.

[9] The GATT agreement made an exception for preferential arrangements that were intended to lead to a customs union or free trade area.

[10] There were special circumstances in 1931 which made depreciation of sterling unquestionably advantageous to the British economy. The currencies of our principal rivals remained pegged to gold until the dollar was devalued in 1933 and the franc in 1936, so that we had an advantage in exports, while our principal suppliers of raw materials kept their currencies aligned with ours (this was the original meaning of the 'sterling area') so that we did not suffer a rise in home prices. There was unemployment and under-capacity working in all lines, so that exports could respond

to an increase in demand. Liberating the balance of payments from pressure made possible a dramatic fall in interest rates and a relaxation of credit that helped to encourage a housing boom. Unemployment continued to grow in 1932 as the world slid deeper into the slump, but the contrast between the recovery that began slowly thereafter with the continued agony of the gold bloc is clear evidence of the beneficial effects of abandoning the exchange rate which the Labour government had destroyed itself to save.

The consequences of the devaluation in 1949 are not so easy to diagnose. At that time the trading world was dominated by dollar scarcity—that is, an overall surplus on the US balance of payments. The UK, as in 1964, was suffering from a growing deficit in the balance of trade. It has been suggested that the US authorities were in favour of devaluation of sterling (see J. C. R. Dow, *Management of the British Economy, 1945–60*, p. 41). The British authorities were hesitant. Their hands were forced by a flight due to the belief that devaluation was in prospect.

It was followed by a marked rise in exports, which, however, lasted for only two years, because the Korean war and U.S. rearmament produced a world boom followed by a recession. The argument that external circumstances would in any case have produced much the same result, and that the long-run benefit of the devaluation was wiped out by money-wage rates rising faster than they would have done if it had not occurred, can be set against the view that exports would have benefited much less by the boom and suffered far more in the long run without its help. At the best, it was by no means such an obvious success as the rupture of the gold standard in 1931.

[11] The EEC (Belgium, France, Germany, Italy, Luxembourg, and the Netherlands, with associates) was initiated in 1957. Beginning on the basis of preparing to set up a customs union—a common tariff against imports from outside—it developed some features of a general economic union administered by a supernational civil service. The EFTA (Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and the UK, with Finland as an associate) was initiated in 1959 with a view to forming a free-trade area—each country to have its own tariff against the outside world but none against each other's industrial goods. The scheme is to come into full force at the end of 1966.

[12] Andrew Shonfield, in *Modern Capitalism*, describes the manner in which the various countries have adapted themselves, each in its own style, to the requirements of national economic planning. French administration and German control through the banks (behind a smoke-screen of laisser faire slogans) permit a high degree of discrimination, between individual firms and between of industries, while we are frustrated by the British tradition that the duty of the civil service is to keep the ring for contending private interests and to see fair play without fear or favour, so that only global controls can be used. 'The economy tended to be treated as an undifferentiated mass with a more or less uniform capacity for response, not as an articulated nervous system which would react very differently to particular stimuli occurring in different places.' (*op. cit.*, p. 101).

[13] In 1963 in Italy personal consumption rose by 10 per cent compared to the preceding year, imports by 21 per cent and exports by only 7 per cent. A severely deflationary policy was adopted with the result that investment was reduced by 7 per cent in 1964. Exports recovered and imports fell. The overall growth rate has been cut from 6 per cent per annum to 3 per cent. The process of absorbing workers from the underdeveloped South into industry, which had been going merrily on, has suffered a setback. This is the orthodox way of dealing with an adverse balance of trade. (*U.N. World Economic Survey, 1964*)

[14] Over the post-war period the United States built up a massive surplus on her balance of trade. She has an unbeatable competitive position in manufacturers because of technical superiority combined with massive unemployment which keeps money-wage rates in check (though the

present war boom is making the authorities begin to think about wages policy). She is the leading supplier of several primary commodities and she has a growing income from overseas investments.

Over the years 1953–5 the surplus on income account was more than offset by military expenditure overseas and public and private capital outflow. The overall deficit was falling during those years and in 1956 and '57 there was a substantial overall surplus. A hard dollar began to be regarded as part of the order of nature. In 1958, in spite of a continuing rise in the surplus on income account, outflows caught up; ever since there has been an overall deficit, making the dollar soft, to the embarrassment of all concerned. (See D. MacDougal, *The Dollar Problem, a reappraisal* 1960. Essays in International Finance, No. 35, Princeton University).

The balance of payments for 1964 was as follows:

	$ millions
Balance on goods and services	+9780
Government military net expenditure overseas	−2060
Grants, etc.	−3120
Private net capital outflow	−6235
Errors and omissions	−1165
Balance of monetary movements	2800

(Bank of Internation Settlements, *Annual Report 1966.*)

[15] In March 1961 the mark was appreciated by about 5 per cent. A surplus on income account for some years had led to piling up of reserves, since the West German financial institutions were not habituated to foreign lending. Usually the monetary authorities of a country do not really dislike amassing reserves, even though it is no good to them and a great nuisance to the rest of the world. Presumably the decision to appreciate was taken under pressure from outside. A truly voluntary appreciation was made by the Netherlands, whose exchange rate moved with the mark. She already had as large a surplus of exports as she had any use for; a sudden boost to exports in her main market and rise in prices for a large part of her imports would have created undesirable inflation. This is a rare case.

III INTERNATIONAL FINANCE

[16] Between 1953 and 1963 the total value of imports was rising at the rate of 7·1 per cent per annum while the stocks of monetary gold rose at 1 per cent per annum. (See R. F. Harrod, *Reforming the World's Money*, p. 71).

[17] Over the same period total reserves were rising at the rate of 2·7 per cent per annum, mainly in the form of dollar balances. Before 1940, total reserves were about equal to one year's total imports. (*Loc. cit.*). In 1964 total reserves of the non-socialist world were $68,970 million, of which $40·860 were in the form of gold. (*UN World Economic Survey 1965*, Part II, p. 49).

[i] See J. M. Keynes, *The Economic Consequences of Mr Churchill* (1925), reprinted in *Essays in Persuasion.*

[j] See above, note 10.

[k] See R. F. Harrod, *op. cit.*, chapter 3.

[l] Keynes' scheme is set out in *Proposals for an International Clearing Union* (1943), Cmd 6437.

[m] The case is argued and connected with the problem of development in *International Monetary Issues and the Developing Countries* (1965), the report of a committee appointed by the United Nations Conference on Trade and Development.

[18] The sterling area, in the modern sense, consists of countries whose monetary reserves are held in London. It corresponds broadly to the Commonwealth and ex-Commonwealth, plus Kuwait and the Republic of Ireland, minus Canada. The greater part of British overseas investment, apart from that of the oil companies, is in areas of the Commonwealth and ex-Commonwealth that are already well developed and offer a profitable market.

[19] It is sometimes argued that foreign lending is undesirable because the investment had better be made at home. This is a fallacy. Home investment is not held back by lack of finance (and if it were, financial remedies could be found). It is held up by lack of labour and other resources, or, to put the same point in another way, it is held up by the need to avoid additional inflationary pressure in a near-full employment economy. To make room for home investment, we should be trying to restrain inessential consumption, not putting obstacles in the way of exports.

[20] 'America as the "land of opportunity" is beginning to lose that title in the eyes of many US businessmen. These businessmen increasingly are deciding that markets abroad —not those in this country—offer the biggest potential for future growth. The feeling grows that the US market, while huge, is relatively "saturated".

'It is overseas that businessmen see the big, untapped market with hundreds of millions of customers waiting—and increasingly able to buy—all kinds of products and services.

'To go after this market, US firms are building and expanding factories all around the world. Since 1958, more than 2,100 American companies have started new operations in Western Europe alone'.

U.S. News and World Report, June 1 1964. Quoted by Baran and Sweezy, *Monopoly Capital*, p. 198.

IV EMPLOYMENT AND GROWTH

[21] Between 1921 and 1938 overall statistical unemployment never fell as low as 9 per cent of the labour force, and, in the worst year of the slump, reached 22 per cent. In some industries the average of unemployment over these years was more than 40 per cent. Beveridge, *Full Employment in a Free Society* gives the history of this experience (pp. 47–69).

Advocating a new policy, he thought it quite optimistic

to argue that unemployment need not be more on an average, good years with bad, of 3 per cent. In fact (apart from the fuel crisis of 1947) the figure for unemployment has not touched 3 per cent since the war, and out of the last fifteen years (up to the crisis of 1966) has been above 2 per cent only in seven. (*Ministry of Labour Gazette*).

[22] While the statistical measure of unemployment for UK as a whole was mainly below 2 per cent, in Scotland it rarely fell below 3 per cent. In Northern Ireland it was sometimes above 10 per cent and has fallen below 7 per cent only since 1964. (*Ministry of Labour Gazette*).

[23] Beveridge's *Full Employment in a Free Society* provides an example of the thinking of that period, rather advanced in its day. He lays down three rules for national finance:

> 'The first rule is that total outlay at all times must be sufficient for full employment. This is a categorical imperative taking precedence over all other rules, and over-riding them if they are in conflict with it. The second rule is that, subject to this over-riding categorical imperative, outlay should be directed by regard to social priorities. The third rule is that subject both to the first and second rule, it is better to provide the means for outlay by taxing than by borrowing.' (p. 147).

The meaning of the third rule is that government investment need not create rentier wealth. In so far as it is financed from taxation the corresponding saving is carried out by the economy as a whole and the wealth created belongs to the nation. To produce a given effect on demand, greater outlay is required if it is covered by taxation, which falls partly on income that would have been saved. The rule entails that, when enough revenue cannot be raised for the expenditure required to maintain full employment, even current outlay should be made from a deficit rather than not made at all.

The second rule applies to the outlay made as a contribution to the employment policy. It is better to do something useful than to dig holes and fill them again, but to dig holes

is better than to do nothing. (The thought that the holes might take a form that was worse than nothing was still blessedly remote). Profit seeking enterprise is to have the first claim on the labour force, government outlay on something or other is to provide employment for the workers that it does not require.

[24] The proposal to cut home demand in order to promote exports is often met (generally by the businessmen concerned) with the argument that a reduction in output for the home market will raise unit costs and so curtail, instead of helping, export sales, and by the argument that exports are the 'overspill from a healthy home market'.

Looked at from a long-period point of view there is some sense in this (though there are many examples of industries specialized to export) but from a short-period point of view it is obvious nonsense. When there is limited capacity in a particular industry, fully occupied, so that delivery dates are long, a cut in one lot of orders makes it easier to fulfil others.

[25] Various estimates have been made of the rate of growth before 1914 and after 1945. These show the latter as appreciably higher than the former. Angus Maddison, *Economic Growth of the West* (1964), gives the rate of growth of output per head of population from 1870–1913 as 1·3 per cent per annum, and from 1950–1960 as 2·2 per cent.

During the latter period no western country except USA and Canada had a lower growth rate than UK. For France the rate was 3·5 per cent per annum, for the Netherlands 3·6 and for Germany 6·5 (*op. cit.* p. 30).

[26] In the old orthodox academic system of ideas exploded by Keynes, the share of wages in the product of industry was determined by the *marginal productivity* of labour. This doctrine is still taught, although it is evidently irrelevant to modern conditions, and indeed never succeeded in getting itself satisfactorily stated, even on its own unrealistic assumptions.

On a long view it is clear that trade union organization,

supported by social legislation, has been an important influence in increasing the share of wages. More immediately, it is influenced by the relation of investment to the propensity to save and by the degree of competition acting upon profit margins. A higher overall level of investment (including outlay on armaments), unless offset by a spontaneous increase in saving, keeps up demand for consumption goods relatively to the supply and so maintains a higher level of prices at given money-wage rates. Weaker competition tends to show itself in higher profit margins and a lower level of utilization of capacity.

Taxation of profits does not raise the relative share of wages, since the corresponding expenditure comes back to profits. An increase in the degree of competition or restraint on prices when money wages are rising increases real wages, but if this goes beyond a certain point it merely creates such a strong seller's market that margins are pushed up again.

There is a catch in the system that prevents any frontal assault on the share of profits from getting very far.

V MONOPOLY AND COMPETITION

[27] The common-law principle that agreements in restraint of trade are not enforceable was much eroded by judgments during the depression. After the war antimonopoly legislation began to be introduced. The Monopolies Commission, set up in 1948, had little effect except in research. The Restrictive Practises Court set up in 1956 deals with agreements and a reconstituted Monopolies Commission examines cases of individual firms which dominate an industry. Resale Price Maintenance was outlawed (with a few exceptions, including the Net Book Agreement) in 1964 under the Conservative government.

[28] A typical example is provided by the case of detergents, which was the subject of a report by the Monopolies Commission in 1966. The Commission showed that for a turnover of £62 million selling costs by the two producers

concerned was £17 million. They recommended a cut in wholesale prices of 20 per cent to be provided for by a cut of 40 per cent in advertising expenditure.

At a press conference which followed the publication of the Report several interesting comments were made. The Aims of Industry said: 'The advertising expenditure of the two main household detergent producers shows how fiercely competitive the industry is.' The chairman of one of the companies said: 'We think the commission have seriously underestimated the role of advertising in the manufacturing and marketing of consumer goods and the great contribution it makes to securing economies throughout the business . . . Exercising her choice in competitive conditions in a free market, the British housewife has struck a good balance between the high cost of unlimited choice and the low cost of no choice at all.' (*The Times*, August 11, 1966).

The argument here is that high advertising costs makes entry into the market impracticable and so secures the economies of scale for the large and powerful firm. It did not occur to the spokesman that to take advantage of low costs by low prices might be an equally effective form of competition.

[n] J. Stiendl, *Maturity and Stagnation in American Capitalism* (1952), analyses the effects of the oligopoly system in terms of US data. A more sympathetic account of it is given by J. K. Galbraith, *American Capitalism* (1957).

[29] Marginal productivity theory suggests that real wages should be kept down to encourage the use of labour-saving methods of production. This would make matters worse by checking the growth of effective demand. Provided that effective demand is kept up, workers dispelled from industry can be absorbed into service trades. This is already happening at a rapid rate. See note 32.

[o] See the Labour Party's Manifestos: *Signposts for the Sixties* (1961), *New Britain* (1964), and *Time for Decision* (1966).

VI WORK AND PROPERTY

[30] The figures for 1964 for the company sector are as follows:

	£ million	
Gross fixed capital formation	2,106	
Increase in value of stocks and work in progress	683	
Gross investment		2,789
Gross saving		2,759
Net contribution of external finance		30

(*National Income and Expenditure*, 1965)

[p] See *General Theory*, p. 156.

[q] Cf. Robin Marris, *Economic Theory of Managerial Capitalism.*

[31] As with the balance of payments, the distinction between the income and capital account in the budget is partly a matter of convention. The underlying conception is that items below the line are those which it is considered legitimate to finance by borrowing, according to ordinary business principles. A surplus above the line represents collective saving. It permits government investment to be financed *pro tanto* without adding to the national debt or permits part of the debt to be retired. According to Beveridge's rules (see note 23 above) the distinction between above and below the line expenditure is not important. What matters is that the total outlay should be sufficient to maintain effective demand.

[32] In 1911–13, 1 per cent of the population owned 69 per cent of property, and 5 per cent, 87 per cent of property. In 1960 the corresponding proportions were reduced only to 42 per cent and 75 per cent. In the latter period, 99 per cent of income from property went to 10 per cent of the population. See J. E. Meade, *Efficiency, Equality and the Ownership of Property*, p. 27. Professor Meade

attempts to reconcile a programme for reducing inequality with a belief in marginal productivity theory.

[33] The *euthanasia of the rentier* was conceived by Keynes (*General Theory*, p. 376) in his vision of a world in which investment had saturated all possible uses for productive capital and the rate of profit had fallen very low. This prospect now seems more remote than it did to him. Rentier consumption, however, could be eliminated while savings out of profits are still needed to finance investment. Dissipation of property by endowment of charities would give the wealth owners a last fling, enabling them to choose their heirs instead of leaving all to the discretion of future governments. In so far as they set about dissaving by dissipating wealth in consumption, there would have to be a corresponding increase of taxation, leading to public saving through a budget surplus, which would be an alternative way of acquiring wealth for the nation.

POSTSCRIPT

The Crisis of 1966

A reserve currency holding volatile foreign deposits, a weak balance of payments, the competition for popularity and mutual recriminations habitual in a two-party democracy, and the existence of a school of thought favouring devaluation, set the stage for periodical financial crises.

In 1964 the Conservative government refrained from imposing deflation in the face of an alarming rise in the deficit in the balance of payments. In spite of apparent prosperity, low unemployment and an exceptionally fine summer, they lost the election in the autumn, though narrowly. The new government advertised the deficit as a reproach to their opponents. This, combined with the fact that the electoral victory had gone to a party called Labour, provoked a flight from sterling. The crisis was patched up by means of international support. Gradually the balances returned and the situation was restored to its original precarious position.

During 1965, the deficit on the balance of payments was reduced until it was a little less than the overseas military expenditure. The government put about a forecast that balance would be achieved by the end of 1966. Their chief reliance (apart from restrictions on overseas investment) appeared to be on a credit squeeze, and on incomes policy.

In the course of 1966 a general rise in interest rates, due to the weak dollar and to anti-inflationary policies in Europe, nullified the effect of the rise in rates in London; it became clear that the deficit in the British balance of payments was not being eliminated, and incomes policy ran into trouble with the seamen's strike. The flight from sterling was renewed. A further turn of the screw in the credit squeeze failed to halt it.

On July 14th the Prime Minister announced that on July 20th he would introduce measures to deal with the crisis. These consisted of an appeal for a general wage freeze (to be made compulsory later if voluntary agreement failed); cuts in proposed public investment; increased taxes on consumer goods and restrictions on hire purchase; and a cut in the tourist allowance of foreign currency. A cut of £100 million in overseas military expenditure and foreign aid was included in the packet. It turned out, however, that the cuts in military expenditure had already been promised in the budget. Only the cut in aid was new.

The Prime Minister declared his intention to preserve the position of Britain as a world power and of sterling as a world currency.

The July measures of 1966, in so far as they were not a mere expression of panic, may be supposed to be designed to operate at three levels—to restore confidence in the sterling exchange rate, to produce an immediate improvement in the balance of trade, and to contribute to a long-term solution of the underlying problem.

So far as the first objective was concerned, the dramatic style in which the whole affair was conducted was more calculated to arouse than to allay the fears of overseas holders of sterling.

So far as the real effect on the balance of payments was concerned, there were two opposite tendencies.

On the one side it seemed that the Labour government was prepared to cause more unemployment than any Conservative government would dare to do. By sufficiently reducing activity at home it is possible to produce a shock effect on imports, stocks being allowed to run down, which can bring about a surplus on income account for the time being. Keeping activity at a reduced level thereafter checks the rise in imports, while there may be some improvement in the situation of exports as a result of slack in the home market.

On the other hand the numerous severe grievances and evident injustices caused by a sudden wage freeze, the opposition aroused in the trade union movement and the piling up of claims for the end of the six months period seemed likely to have a negative effect on wage restraint, which might not be offset by the rise in unemployment.

The contribution to the long-term problem of the July measures was wholely negative. Cuts in investment, the rupture of productivity agreements required by the wage freeze and the renewal of the restrictiveness of trade-union mentality engendered by reviving fears of unemployment threaten a reduction in even the slow rate of growth which was the basic cause of the poor performance of the British economy in recent years.

The one hopeful feature of the situation is the growing support (not only on the left) for the point of view expressed in the *Conclusion* above. Perhaps in the end the facts of life, like a sheepdog with an awkward flock, will finally nudge democracy towards common sense.