Wage Policy To-day and To-morrow

by

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While theoretical economists hold that the determination of the level of wages should be left to the free play of the law of supply and demand, observation of the facts suggests that this law has been rendered inoperative by the action of a certain number of non-economic factors which oblige the State to intervene in the matter, whether it likes or not. If the necessity for State intervention is admitted, a question of capital importance is the direction of this intervention. In other words, what should be the nature of the wage policy to be adopted by the State? Is it to be directed to raising, lowering, or stabilising the income of the working classes? The author of the following article does not think that these questions can be given an absolute answer; the decision must depend on the circumstances of each case. Studying more particularly the conditions of the present phase of economic fluctuations and the recovery that seems to be in prospect, the author tries to determine the attitude to be taken by the State at each stage of events in the interests of the economic system in general and of the workers in particular.

I.

THERE has been something tragic about the history of social policy in the last fifteen years. The war caused so much human suffering in all the belligerent countries—among victors and vanquished alike—that European public opinion in 1919 was ready to seize any opportunity of giving the masses of the population some compensation for the sufferings and sacrifices of the four war years. Never had the prospects of attempts to improve the position of the workers seemed brighter than at that still comparatively recent date. The standard of living of the majority of the population was rising rapidly and continuously; wages were soaring; and this increase in the direct income of the workers was accompanied by an extension of the indirect services provided for the workers by the State : social insurance in all its branches and public welfare work of all kinds developed quickly. But this period of extremely rapid and extensive improvement in the conditions of industrial workers was followed by a sudden and violent relapse. At no period in modern social history have the workers' living conditions undergone so abrupt and so marked a change for the worse as during the past five years. This relapse, following a period of intensive progress, became catastrophic in some countries; it has now come to a standstill, but social policy has not yet wholly recovered from its psychological effects. The decisive factor for the future of social policy will be whether there is sufficient intellectual resistance behind it to survive this practical defeat and hold fast to its sound theoretical foundations.

The danger undoubtedly exists. The opponents of social measures find it easy to make capital out of the chance historical sequence of rapidly extending social policy and the worst depression the world has known. The present article, however, is not concerned with discussing whether the efforts made to raise the standard of living of the masses are or are not responsible for the economic collapse. This problem belongs to the past ; for the present and the future what is more important is the assertion that the time has gone by when the State could attempt to influence the economic conditions of life of the workers. In many countries of Europe, at least, this view is very widely held, because social policy can easily be confused with a thousand other forms of State intervention in various aspects of economic life, and the natural distaste of industrialists and individuals for tariffs, quotas, currency restrictions, and the like can easily be transferred to social policy. The demand for economic freedom is so often thoroughly justified on economic grounds that it is the more important to defend the activities of the State in other domains of economic life against unfounded criticism from liberal quarters.

This article proposes to deal with only one branch of social policy, but one of the most important, namely, State adjustment of the level of wages. No attempt will be made to discuss the technical means by which the State can do this ; it is not the method that is being examined, but the most general principles of wage policy. The actual machinery of wage adjustment is in any case relatively unimportant in an analysis of the proposition that the State should, in principle, abstain from influencing wages in any way whatever. This assertion has been made with growing emphasis for some years past, and it is all the more worthy of attention because it is made not only by those directly concerned but also—and at least equally strongly—by economists. The thesis put forward is that wages must once again be made subject to the influence of the forces that naturally determine them, which are in fact the laws of a free economy.

How the free play of economic laws determines the level of wages is common knowledge and can be dismissed in a few words. [1] The most general principle of these laws is that, other things being equal, the lower the wage the greater the number of workers employed. If pressure exerted by the State or the trade unions to bring the level of earnings of the individual worker above the natural level is withdrawn, employment and production will increase. This theoretical assertion is supported by two facts, apart from certain minor considerations. The first of these facts is the connection between the total volume of production and the ratio of prices to costs. At any given price level any increase in the cost of production is bound to lead to a decline in the volume of production; if wages are raised, certain undertakings will cease to work at a profit and will therefore collapse, and the result is unemployment. The second argument in support of the theory that wage movements and unemployment follow parallel courses is to be found in the relation between the level of wages and the technique of production. The lower wages are, the less inducement is there to replace human labour by machinery, and the less, therefore, will be the danger of unemployment as a result of rationalisation. In this general form both these arguments are undoubtedly sound, and the conclusion drawn from them is therefore logically unassailable. At first sight, indeed, it seems that, if other economic conditions remain unchanged, a rise in wages would probably produce unemployment and a fall in wages would reduce unemployment. This argument is therefore used to support the demand that the fixing of wages should be left to the free

[1] Here and subsequently the writer has tried to avoid all technical terms of economic theory. The natural result is that many of the finer points of the argument cannot be brought out.

play of economic forces, which would ensure the stabilisation of wages at their natural level.

What is the " natural wage " ? Here again the answer is simple : it is the level of wages at which there is no unemployment. The actual wage cannot be higher than this, or masses of workers will be condemned to involuntary idleness; nor can it fall lower if economic forces are given free play ; if it did, it would be raised again by competition between undertakings to the level at which supply and demand on the labour market were in equilibrium.

The core of all liberal criticism of State intervention in the field of wages is this claim that if wages were fixed freely by competition on the labour market unemployment would be removed. The first question to be answered when considering whether this criticism is justified or not is whether there is really any prospect of this claim materialising. The problem is absolutely fundamental. If the determination of the level of earnings of the bulk of the population is to be removed from the sphere of influence of the State and left to the free play of economic forces, there must be some guarantee that the forces of the free market are able to determine a quite definite level of wages based on purely economic considerations. But a level of wages determined exclusively by economic conditions exists only when every worker is in employment, for otherwise wages would have to fall still lower. In other words, the opponents of a State wage policy are right only if a free labour market does actually mean the abolition of unemployment. Half results in this matter do not count at all. However great the reduction of unemployment under a system of free competition, this is no condemnation of a State wage policy so long as the aim of employment for every worker is not reached. The system of free economic competition will have vindicated its principle of wage determination only when there are no more unemployed at the employment exchanges ; so long as any appreciable unemployment still exists, wages are not regulated by purely economic considerations.

What then are the other factors determining the level of wages in such circumstances ? They may differ from case to case; their only common characteristic is that they are not solely economic, but are also to a great extent social factors. This is true even when wages settle at the limit of the minimum of physical subsistence. For even the minimum of physical subsistence has ceased to be a biological quantity ; even in its narrowest sense it must be taken to include a certain number of habits of life, intellectual and spiritual needs, and so on. The social element in the determination of wages becomes particularly clear in a period of unemployment, when the fall in wages reaches a limit below which the opposition of the workers, the anxiety for social peace, or the strength of public opinion refuses to let it pass. These are all sociological facts ; they are the typical factors that play a decisive part in determining the wage policy of States—the various social reactions of different groups, which are co-ordinated by the State as the executive organ of the collective will and put into effect in its policy. [1]

The next question, therefore, is whether there is the slightest probability that the complete and unqualified abolition of all State efforts to control the level of wages would render these social factors inoperative on the labour market. It was pointed out above that wages are not determined exclusively by economic factors until unemployment has entirely disappeared. [2] The above question can therefore be put in another form : is there any probability that the removal of all political influences from the labour market would lead to the disappearance of unemployment within any reasonable time ?

If the question really refers only to the near future, to the next few years, then the answer is almost obvious. It has been said that even a negative wage could not end the present unemployment. There is no need to test the accuracy of this exaggerated statement of the case here. The possibility can be left open that an unusually low wage of a few pence an hour might really put an end to unemployment. But such a wage is clearly impossible ; there are in fact things in modern economic life against which the logic of pure economic theory breaks down, because it comes up against insuperable sociological barriers. A fuller explanation will be given later of why it is improbable that even a considerable reduction of

[1] The writer has tried to analyse the effects of social factors on wages in greater detail in an article entitled " Lohn und Konjunktur vor dem Kriege ", in *Archiv für Sozialwissenschaft und Sozialpolitik*, Vol. 62, 1932.

[2] Although it is necessary to lay such emphasis on the complete disappearance of unemployment in this connection, as contrasted with a mere partial improvement of the situation on the labour market, this does not mean that " statistical unemployment " must fall to zero before wages are determined solely by economic factors. It is recognised—as Beveridge was the first to point out in the first edition of his classic study, *Unemployment*—that even in the periods of greatest prosperity before the war unemployment never entirely vanished.

wages would abolish the present unemployment. For the moment it will suffice to point out quite generally that we are in an unusually deep and unusually prolonged depression. It is clear that greater efforts and more time will be required to recover from a depression of unprecedented intensity than to remedy the effects of a slighter slump. It is also beyond dispute that special historical phenomena—more especially the political unrest in the world of industry—stand in the way of recovery on this occasion. And what is true for the economic system in general holds good also for that section of it with which we are here concerned, namely, the labour market.

In addition to cyclical unemployment, however, there is another kind which there is even less prospect of removing in the near future. This is technological unemployment. Its extent is not definitely known, but it is at any rate an advance that its existence is slowly coming to be generally recognised. [1]

It is possible that we are at the beginning of a period of gradual economic recovery, that the number of unemployed will fall in the next few years, and that a suitable wage policy might help on this process. But the sad conclusion remains beyond dispute that not even the most drastic reduction of wages could remove unemployment completely in the near future ; its extent is too great and the effect of wage reductions —as will be shown later—too uncertain. So long as there is a surplus of labour on the market, the wage level is not being fixed by purely economic factors. It appears that at no period of modern history has the economic mechanism of free competition been less able to determine the level of wages unaided and by its own laws than it is at present. This conclusion is a direct consequence of the fact that the abolition of unemployment has never been such a huge task as it is to-day, and that the instrument of wage reductions has been proved by experience to be insufficiently effective. It must be borne in mind,

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[1] It has taken a long time for the world to realise that permanent unemployment may possibly result from the rationalisation of industry. The International Labour Office has done very valuable work in spreading a knowledge of this truth. Cf. in particular : H. B. Butler : *Unemployment Problems in the United States* (Geneva, 1931), chapters III and IV ; *The Social Aspects of Rationalisation* (Geneva, 1931) ; and the discussion between Professors Bouniatian and Lederer in *International Labour Review*, March and July 1933. Cf. also : E. Lederer : *Technischer Fortschritt und Arbeitslosigkeit* (Tübingen, 1931) ; A. Kähler : *Die Theorie der Arbeiterfreisetzung durch die Maschine* (Leipzig, 1933). The contrary opinion is expounded by N. Kaldor in "A Case against Technical Progress", in *Economica*, May 1932.

too, that a State wage policy and the power of tradition and public opinion are not the only obstacles to the fixing of wages by the methods of free competition. The ideal situation, as envisaged by liberal economists, is not attained unless there is also free competition on the demand side; and it is practically a commonplace that at no period in the modern industrial age has this competition been more fettered than it is to-day as a result of the concentration of undertakings, the organisation of cartels, etc. One may agree with liberal critics in deploring this state of affairs, but it is doubtful whether their criticism will be effective enough to change matters in the near future.

It is not by arbitrary choice, but under compulsion, that States embark on a wage policy. If they gave it up, they would soon be driven back to it, because there is no sociological principle that can relieve them of this necessity. Free competition on the labour market is no alternative, because free competition does not exist and cannot, in the form required by pure theory, be created at the present time. In a period of continued depression and chronic unemployment on a large scale the free mechanism of the economic system cannot take over the full responsibility for wages; it is for this reason that the responsibility of the State for the level of income of the mass of the people has increased so enormously. The assertion that the period for the intervention of social policy on the labour market is over must be countered by the contrary assertion that there have perhaps been few periods when the outlook for social progress was so black, but equally certainly none in which social policy had a greater burden of responsibility to bear.

II.

Willing or unwilling, the State has wage policy under its control. How is this instrument to be applied? The greater and the more exclusive its influence on the level of wages, the more important it is to be certain that the method is the right one. This is a problem of political economy, and in the following pages it will be studied with the help of political economy. This means that a certain amount of economic theory is unavoidable; the excuse for this is the importance of the matter. The theoretical discussion will be kept in very general terms; as it is not the concrete situation in one country that is being studied, but the outstanding features of the international situation, no detailed conclusions can be expected.

State wage policy is economic policy and social policy at the same time. The aim of economic policy is to promote favourable economic conditions or, reduced to a simple formula, to raise the national income. Social policy aims at improving the situation of the economically weaker strata of the population; it too endeavours to raise a collective income, but it is the income of only one section of the population—the workers. It is not always possible to achieve both these ends by the same means, but a measure that improves the economic situation of the workers rarely harms the other sections of the population, and *vice versa.* Here, however, the question must be looked at exclusively from the standpoint of the workers' well-being. The well-being of the workers means the highest possible level of wages, combined with employment for the largest possible number of workers. But we have seen that these two do not always go together: a rise in wages implies a risk of increased unemployment, while a fall in wages may lead to more employment. If, for social reasons, the latter course is preferred, wage policy will be in harmony with general economic policy, as it will increase the total volume of production and so raise the income of the other classes of the population. If in the interests of the workers it seems preferable to raise wages, even at the cost of the volume of employment, then social policy and general economic policy come into conflict with each other.

The number of conflicting interests involved is obviously large. Even from the point of view of social policy alone a large number of interests must be considered in choosing between lower unemployment and higher wages. The number is still greater for the general policy of the State, which in all its measures has to look after the interests of every group of its citizens. The centre of the problem lies in the initial assumption of a connection between the level of wages and unemployment. The questions raised cannot be answered until this connection has been more closely investigated. We must therefore first examine the effects of a change in the level of wages on the volume of employment and production in the present period of depression.

The general conditions in which the problem of wage policy is rooted differ not only from country to country, but also from industry to industry, and even from undertaking to undertaking. For the purpose of the present article, therefore, the characteristic features of the economic situation may be summed up as follows. The depression has passed its lowest point; the contraction of production and sales has stopped; there are faint signs of renewed activity, but the upswing has not really yet begun. For some little time the level of wages has also remained stationary. Given these circumstances, what will be the effect of lowering or of raising wages on the level of employment?

According to the theory of the connection between the level of wages and unemployment, there are two reasons why a fall in wages is likely to relieve the labour market. The first is that when wages are low there is less incentive to introduce labour-saving machinery. Even in the present situation this argument is logically sound. The only doubtful point about it is the extent to which wage changes can in this way affect the level of employment. The technique of production, especially as regards the ratio of men to machinery in the productive process, cannot be changed in a day. It depends essentially on the mechanical equipment of the undertakings. In periods when the technical equipment of industry is being developed or when much old plant is being scrapped and replaced by new, the question of the ratio of men to machines in the productive process is settled for some considerable time to come. If industrial plant were being extensively developed and transformed at the present time, then it might be argued—especially in view of the disastrous effects of rationalisation on the labour market—that a fall in wages would serve to ward off more serious dangers. But in reality there is not at present much activity in the domain of technical equipment, nor is there likely to be for some time to come. Expansion and the substitution of new plant for old are the characteristic concomitants of a period of rising economic prosperity; they were never so marked as in the boom period of the years before 1929. Then, it is true, relatively high wages were one of the motives for mechanisation, which reached such a pitch that later on it had most deplorable social consequences. But the expansion of the mechanism of production during those years was so tremendous that industry entered the depression with an unprecedented excess of productive capacity. This great excess of capacity is one of the main obstacles to the beginning of a new business revival, because it deters undertakings at present—and will presumably do so, though to a less extent, for some time to come—from any fresh capital expenditure. But this circumstance also means that the present level of wages will have comparatively little effect on the extent of future technological unemployment.

It is only slowly, and by a very complex process, that wage movements exert an influence on the technique of industry, and thus indirectly on the level of employment. Because the process is so slow, especially at the present time, there is the less need to fear its consequences. But the other argument in support of the alleged connection between wages and unemployment—the relation between costs and prices—is of more decisive importance. Wage changes naturally have an immediate effect on the general cost of production, and this very quickly reacts on employment. This aspect has therefore rightly been kept in the foreground in all decisions of wage policy.

If wages are lowered, the cost of production falls; if prices remain unchanged, firms that were formerly unable to make a profit can now resume production. It is possible, by going a step farther, to extend the connection between a fall in wages and employment. If wages fall in a single industry, it is highly probable that competition will compel the undertakings to lower their prices correspondingly. But the fall in prices should increase sales, for when a commodity becomes cheaper there is a tendency for consumers to purchase more of it at the expense of other goods. A reduction in wages that is restricted to one industry—the case usually considered by economic theory—will certainly lead to the employment of more workers in that industry. It may even be asserted that the increase in the volume of employment due to a fall in wages in one industry at the present time would be especially large. Undertakings react to a fall in wages because it means lower costs. But the same reduction in wages does not always mean the same fall in the cost of production for the undertaking. In times of prosperity undertakings are often overworked; any further increase in production intensifies this overwork, and the cost per unit of output therefore rises with the volume of production. In a boom period the inducement to increase production, and therefore employment, offered by a fall in wages is counterbalanced by the fact that the existing organisation of the undertaking makes it increasingly difficult and expensive to produce more. In times of prosperity, therefore, the fall in wages must be very considerable before it will lead to any appreciable increase in the volume of employment ; the influence of wage changes on employment and unemployment is then slight. [1]

During a depression matters are reversed. At present most undertakings are suffering from a decline in demand, which makes it impossible for them to use their plant to the full. At the peak of the boom period industry was being run uneconomically because too much was produced ; now it is being run uneconomically because too little is being produced. The plant is not working to capacity ; if more workers could be employed the cost per unit of output would be reduced. The stimulus to increase production offered by a reduction of wages in a single industry is thus strengthened by the accompanying reduction of costs. And the more marked the downward movement of unit costs, the greater—for a given increase in demand due to falling prices—will be this stimulus. But costs fall more quickly as production increases if the undertaking has been working far below capacity ; they will therefore fall especially sharply in the present period of deep depression. It will be seen, then, that a single industry is justified in claiming that a reduction of wages at the present juncture would enable it to increase its staff very considerably.

But the general principles of wage policy are not applied to individual industries. The immediate aim of wage policy is to influence the level of wages in every industry ; if, without any special reason, the State lowered wages in one industry, thus giving it the advantages resulting from the possibility of employing more workers, it would, from the point of view of economic policy, simply be making a gift to that particular industry. It was pointed out above that the increase in production that follows a fall in wages in a single branch of industry is partly due to the fall in the price of its products which diverts consumer demand to them from other goods. To present a single branch of industry with the advantages of a wage reduction is therefore quite unfair : the advantage to this branch is gained at the expense of others, and the increase in employment in the favoured industry will be balanced by dismissals elsewhere. This is one reason why the value of a fall in wages, from the point of view of political economy, at once seems

[1] This point was recently very forcibly made by Professor Pigou. Cf. *Theory of Unemployment*, p. 89.

doubtful. The other lies in the danger of the reduction of purchasing power that results from a decline in wages. So long as the reduction of wages is considered within the limits of a small branch of the economic system, this danger is not great. The workers in the boot and shoe industry, for instance, purchase such a small fraction of the shoes they manufacture that a fall in their income has no appreciable effect on the position of the shoe industry. But when the general level of wages is in question, the purchasing power argument begins to assume considerable importance. It is an argument that must now be examined more closely.

If wages are reduced over the whole of the economic system and if prices fall with the consequent decline in costs, the best that can be hoped for is that the level of employment will not be affected at all. The aggregate price of all the goods produced will have fallen by the same amount as wages have been reduced; aggregate income will have fallen by the same amount; and the same volume of commodities is purchased and produced as before, but at a lower price. Yet the process is not entirely negligible in its consequences, for the percentage fall in prices will be less than that in wages, since costs include not only wages, but also a number of other elements, which remain constant. The real income of the workers will fall, while other classes of society, whose money income has remained unchanged, can buy more at the lower prices. It is to be hoped that they will do so! If they do not spend as much as before, but merely purchase the same quantity of goods at the lower prices, there is nothing to counterbalance the decrease in the effective demand of the workers. This is by no means an improbable case. In periods of rapid capital development, any sums of money saved, as a result of the fall in prices, by groups of the population other than the workers could pass through the banks and go to create effective demand in the hands of industrialists. But at present there is little prospect of this process occurring with any degree of rapidity, in view of the existing aversion to capital expenditure. If no such effective demand is created, the whole result of the lowering of the wage level is a reduction of the aggregate demand for commodities, an incentive to a further contraction of production. Instead of lessening unemployment, the fall in wages will have increased it.[1]

[1] On this point, cf. an article by R. F. HARROD in *Economic Journal*, March 1934, pp. 22 et seq.

But it is by no means certain at the present time that the reduction in costs due to a fall in wages will be fully reflected in prices. There are too many undertakings working at a loss, and they will welcome the lowering of their costs simply as an opportunity of again making a profit, or at least of lessening their losses. Further, the reaction of industry to any change in economic conditions is very largely determined by psychological factors. In the early years of the depression it was hoped that a reduction of prices would improve the situation, but now the policy of reducing prices is quite out of favour, and the raising of the price level is hailed as the first and essential condition for a revival of trade. If wages drop and the existing level of prices is maintained, the result will be different. If the income lost by the workers is spent in the form of increased income of other sections of the community, there will again be no change in the volume of production or of employment. But this is only one side of the process ; this simple picture of a transfer of income from the workers to other groups of the population refers to a section of industry that was actively engaged in production even before wages fell. But if wages fall and prices remain unchanged, undertakings that had to close in consequence of the collapse of prices during the depression will be able to work at a profit and will open their doors again. This is the process that the advocates of wage reductions always emphasise. Lastly, the higher profits or smaller losses in undertakings that were still producing before the reduction of wages have also a good psychological effect, and anything which tends to restore the confidence of industrialists and improve their view of future prospects is a far from negligible gain at a time like the present, when initiative on the part of the leaders of industry is one of the most important conditions of economic recovery.

A fall in wages without a simultaneous fall in prices has therefore some chance of increasing the volume of employment, but only under certain definite conditions. The primary effect of any reduction of wages—before the secondary effects set in—is to decrease demand. This negative consequence is not dangerous if it is offset by other positive consequences. In the case just considered, which is the one most closely resembling the present situation, the workers' loss of purchasing power would require to be counterbalanced by a corresponding increase in the expenditure of other sections of the population. This is essential if undertakings that were closed are to resume production and thus create more employment. Theoretically, it is possible to make good the loss of the wage earners' purchasing power : a commodity that cost one dollar before wages fell will continue to cost one dollar, but the fraction of the cost representing wages will fall from 50 to 40 cents, and the 10 cents difference will be spent by the industrialists and the shareholders instead of by the workers. The whole process is merely a transfer of income—always provided that the non-workers spend the extra 10 cents as soon as the workers reduce their purchases by that amount. If this does not occur, the negative effect of the wage reduction precedes the positive one, the aggregate demand falls, and a process of contraction sets in.

Now, it is highly improbable that the non-workers will increase their demand simultaneously with the restriction of consumption by the workers. The primary fact when wages are lowered is that the purchasing power of the workers falls, and this fall makes itself felt not later than a week after the reduction of wages. As a rule, the other groups of society will not begin to spend more until their income has risen, and this cannot occur until production has continued for some time at the old level after the reduction of wages. They will therefore wait some time before increasing their demand for goods, and while they are waiting the reduced purchasing power of the workers affects the volume of commodities sold. Production will then begin to fall, and once this occurs it is no use hoping for increased expenditure by the non-workers, for it will not materialise.

The process will not necessarily take this course at every phase of the business cycle. If the spectre of the depression has passed from the minds of industrialists and is replaced by a definite feeling of optimism, then the mere prospect of wage reductions, or the expectation of greater profits in consequence of a reduction of wages that has been decided upon and will shortly take effect, may possibly lead undertakings to increase their expenditure before and concurrently with the reduction of wages. This is especially so in the case of capital expenditure on machinery and raw materials. But an improvement in the demand for means of production requires to-day a very strong incentive; it is hardly likely to be brought about by a mere prospect that profits will increase on the assumption that the volume of production remains constant. But if a decline in the sales of most undertakings is the first consequence of a fall in wages, even undertakings that would otherwise regard the reduction of wages as a reason for resuming production will think twice before they take the risk of doing so.

During the process of economic contraction which still characterised the economic life of most countries up to a year or so ago good reasons could be found for lowering wages. What was required then was to check the growing decline in demand by lowering prices and maintaining the level of employment at the cost of the incomes of the working masses. Even here the policy of reducing wages cuts both ways, because it leads itself to a fresh fall in demand, but there are situations in which it may be justified. This period is fortunately past; in most countries the decline in the volume of production and of employment has stopped, and demand and the present volume of production are in unstable equilibrium at a very low level. The instability and insecurity of this situation after several years of contraction are obvious, and it is just for this reason that it is dangerous to interfere. Enough has now presumably been said to show how great would be the danger of disturbances if wages were lowered. But these dangers are not perceptible unless the whole of the economic consequences of a general reduction of wages are taken into account. From the point of view of a single undertaking or a single industry, the advantages of a reduction of labour costs are undoubted, which explains why so many people are honestly convinced that the policy of reducing wages should be continued.[1] Unfortunately, in theoretical discussions the dangers of wage reductions are often overlooked, but they none the less exist in practice. The prospect of increasing the volume of employment by a general reduction of wages is at present very slight, and there seems to be no justification, either social or economic, for any further reduction of wages.

This conclusion, as was pointed out above, holds good for the general economic situation in most countries at the present time. Extraordinary circumstances may invalidate it. Only one exceptional situation of this kind can be mentioned here, but one which is very much in the public eye at the moment.

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[1] The opposite error is naturally also common. "It is ... easy to see why Trade Unionists bother so little about the connection between their wage policy and unemployment. The unemployment caused by their policy does not appear at once, but only declares itself gradually.... The unemployment which is actually the result of the original advance will only show itself when the plant comes to be renewed, or as the marginal firms die off and there is none to replace them. Thus to the Trade Unionist wages and unemployment naturally appear to have little connection." (HICKS: *The Theory of Wages*, p. 184.)

The devaluation of foreign currencies may place a country that wishes to keep its currency stable at a very great disadvantage on the world market. The result is that it tries to lower the prices of its products in terms of foreign currencies, since these appear too high on the international market because of the devaluation of other currencies. This can be done in two ways : either by following the foreign example and devaluing the currency, or by forcing down internal prices. We need not here discuss the much-debated question of which method is preferable ; only the second is of interest for our purpose. If it is decided to reduce prices, then wages must also be lowered. This lowering of wages—if other considerations of economic policy are left out of account—is not open to the same objections as the wage reduction discussed above, for which there was no special motive. But it escapes these objections only if it is really a component part of the general process of deflation —i.e. if money wages fall in the same proportion as prices and there is no reduction of real wages. From the point of view of foreign trade a lowering of real wages would also be useful. In none of the larger countries, however, is foreign trade of more importance than the home market ; and as wage reductions could not be restricted to the production of goods for export, the harmful consequences, described above, of a unilateral reduction of wages would soon be felt on the home market, and as a rule would probably outweigh the favourable consequences of forcing down wages in the exporting branches.

A policy of wage reduction is here rejected because it gives no promise of an increase in employment or production in the present circumstances. Does this mean that a policy of raising wages is desirable ? Would a rise in wages—this is the economic question—cause an increase in employment instead of a decrease, as is generally assumed, or may it be expected—and this is the social aspect—that the decline in employment would be so slight as not to neutralise the advantage to the workers of the rise in wages ? The answer is again in the negative. Closer examination will show that a rise in wages also cuts both ways : it increases demand among the workers, but it reduces it among other sections of the population, and creates a danger that undertakings may have to close down because the rise in wages so upsets the balance between costs and receipts that there is no point in continuing production. In the case of a reduction of wages the positive effects were doubtful ; they might not materialise because of the probable disturbances that would result. In the case of a rise in wages the negative effects are by no means doubtful—they can be definitely expected. We have already seen that if wages are reduced the future increase in profits will not cause the non-worker sections of the population to increase their expenditure until the profits have actually materialised. But undertakings will not wait to close down until they have been running at a greater loss for some considerable time. The consumer does not increase his expenditure until his income has actually risen ; the undertaking works on the basis of calculations. If the calculations show that the higher costs are involving intolerable losses, the undertaking will close at once rather than run at a heavy loss for some months until the calculations have been borne out by experience.

Thus, while there is no economic justification for lowering wages, there is still less reason for raising them. So long as there is no change in the economic situation as a whole, the wisest policy appears to be to keep wages at their existing level. Does this mean that the present wage level is in any economic sense the correct one ? It is impossible to answer this question in the affirmative, if only because the wage reductions in different countries during the depression did not in any way correspond to the gravity of the economic situation in the various cases. In addition to national economic considerations, historical factors of a more or less accidental nature also played a certain part, such as the power of the various social organisations, the development of internal policy, the general trend of public opinion, etc. Where these social phenomena really led to the commission of grave economic errors, an appropriate wage policy may be useful to-day as a corrective. But, apart from certain exceptional cases, minor differences in the movement of wages in the different countries are unimportant, for it must be recognised that economic science is still far from having reached that degree of accuracy and reliability that would enable it to say whether a somewhat higher or lower level of wages was " right ". We cannot therefore make such an assertion about the general wage situation either. The only answer that can be given is the negative one that in general wage changes offer no prospect of success. Positively speaking, this means that in most countries the economic system seems to have accustomed itself to the present level of wages and that the stabilisation of economic conditions at the present low level renders any new process of adaptation unnecessary.

III.

What has been said above applies to the period of economic stagnation through which most countries are now passing. Fortunately there is some reason for studying the same question for a period of economic revival. The end of the process of contraction is in itself an earnest of the dawn of recovery. On this occasion it is taking longer than usual for the curve of the business cycle, after falling for some years, to pass the bottom of the trough and begin to rise again. But there are many signs in various countries that recovery will soon begin, even if with some hesitation and frequent relapses. In Great Britain, the United States, some of the Dominions and Scandinavia the recovery already is or has been in progress; there is every prospect that it will grow stronger or begin again in the near future.

Whenever and in whatever form the upswing may begin, one thing is certain: it will not be started by intervention in the domain of wage policy. This is not a peculiar feature of the present phase of the business cycle: changes in the purchasing power of the masses may influence the form and nature of a recovery, but they cannot give the initial impulse. Now as ever the incentive must be given by increased capital expenditure, unless—but this is an exceptional case—it is given by a favourable turn in the foreign trade of a country, as was the case in 1926, when the British coal strike was the starting point of Germany's economic recovery. Increasing capital expenditure may result from the need for new plant in certain undertakings, from a wish to apply some particullary effective new technical process, or—an especially important cause to-day—from housing schemes or other measures taken by the public authorities to create employment.

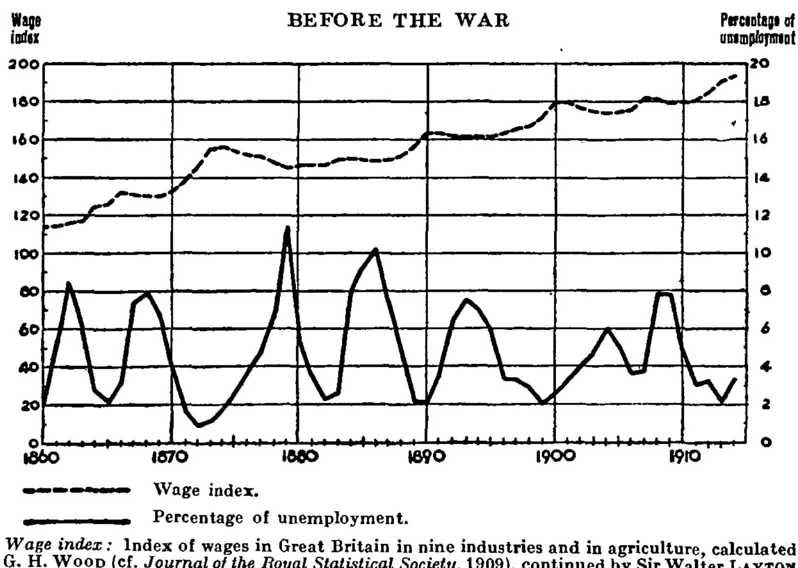
The beginning of the process will be slow. The experience of the last couple of years shows that no rapidly spreading recovery can be expected, for even the most strenuous efforts made by Governments to start the process of recovery have led to only very modest progress, often followed by further periods of stagnation. A slow rise in production means a slow improvement in industrial profits. Industry will become more profitable even if prices do not rise, and there can be no hope of a rapid rise in the price level when sales are slow in increasing.[1] But profits will improve even if prices remain constant, for the great majority of undertakings will for some little time be working

[1] This does not apply to commodities on the world market, such as copper, cotton, wheat, etc., which, however, are of no moment in this connection.

under the law of diminishing costs—of course provided that wages do not rise. The next question, therefore, is whether wages should be kept unchanged even when the recovery is beginning.

The problem of wage policy in the coming years of economic reconstruction is of much more fundamental importance than might appear from the above question. Even those who believe that the upswing will soon begin anticipate that it will be a much slower process than on similar occasions in the past. On the other hand, it is well known that relative unemployment is to-day much greater than ever before. It is probable that even if the recovery process continues uninterruptedly for years the number of unemployed will still remain very high. And so long as there is any appreciable amount of unemployment there is no direct economic incentive to raise wages. The price level on the labour market, as elsewhere, depends on supply and demand: there must be a shortage of labour before its price can rise. In fact a study of earlier recovery periods shows that wages did not begin to rise until the supply of labour on the market reached a certain minimum. The course of the English business cycle before the war may be taken as an example.[1]

THE LEVEL OF WAGES AND UNEMPLOYMENT IN GREAT BRITAIN BEFORE THE WAR



Wage index: Index of wages in Great Britain in nine industries and in agriculture, calculated by G. H. Wood (cf. *Journal of the Royal Statistical Society*, 1909), continued by Sir Walter Layton (cf. *Introduction to the Study of Prices*, London, 1912), for the period 1902-1910 and brought up to 1914 on the basis of the Board of Trade Index. (Base : 1850 = 100.)

Unemployment: Percentage of trade union members unemployed. (*Abstract of Labour Statistics* for various years).

[1] More reliable statistics of wage movements and unemployment over a fairly long period are available for England than for any other country.

A glance at the diagram shows that during the first stage of each upward movement wages in most cases remained almost unchanged, although unemployment decreased : wages in fact lag behind the improvement in economic conditions. It is only when relative unemployment reaches a certain lower limit that the level of wages begins to rise ; it then improves more rapidly as the remaining unemployment is absorbed. In Great Britain before the war, the wage level began to move when unemployment had fallen to about 4 or 6 per cent. Let us consider for a moment what the labour market is like when unemployment reaches this level. It is clear from a glance at the diagram that unemployment never falls below a certain fixed limit, which in Great Britain was never less than about 2 per cent. even when there was an urgent demand for labour. The residuum does not represent a surplus labour supply ; it is the statistical expression of the continual movement of workers from one job to another, partly because of the workers' desire for change, partly as a result of processes of adaptation in the economic system. Genuine unemployment at the moment when the wage level begins to rise must therefore be considerably lower ; in Great Britain it must have been between 2 and 4 per cent. Now it is only in theoretical discussions that all workers are equal ; in reality they differ very greatly in their capacities. It may therefore be safely assumed that when the percentage of unemployment falls so low only workers of poorer quality will in general be available. All this is sufficient proof that in the normal course of the business cycle the wage level does not begin to rise until there is a real shortage of good workers on the market.

Let us now examine the present situation in the light of this conclusion. At the end of 1934 the proportion of workers unemployed, according to the trade union statistics, was—to take only a few examples—14.9 per cent. in Great Britain, 21.4 per cent. in the United States, 14.1 per cent. in Germany, 18 per cent. in Canada, 20.4 per cent. in Australia, and 17.8 per cent. in Sweden.[1] The difference is one of quantity, but it also implies a difference of quality. As regards the possible rate of decrease of unemployment, Great Britain may again be taken as an example, for a marked process of recovery has been going on there for more than two years. In spite of this, unemployment only fell from 17.6 per cent. (average for the

[1] Cf. *International Labour Review*, Vol. XXXI, No. 2, Feb. 1935, pp. 245-248.

year 1932) to 13.9 per cent. (average for 1934). These figures only go to confirm the conjecture made above that the best that can be hoped for in the next few years is an increase in employment, and not the disappearance of unemployment. If therefore the State decided to raise wages when the economic situation improved but before unemployment on a large scale ceased to exist, the old relation between wage movements and the business cycle would be destroyed.[1] Wage policy would then cease to follow the course that it would necessarily take under free competition; it would be aiming at something fundamentally new. Whether and how far such a development is acceptable will be briefly considered in the following pages.

It is obvious that the most general principle of wage theory, that " the lower the wage, the greater the probable volume of employment ", suggests that wages will not rise until the reserves of the labour market are exhausted. But we have already seen that such general formulae as this do not go far enough. If the problem is to be studied in detail, it must first be stated with more precision. We are considering a gradual improvement in economic conditions, and we have seen that even a slight increase in sales would definitely improve the situation of industry, because increasing production means falling costs and therefore higher profits. The question then is whether these higher profits should be used to increase the workers' incomes. There can of course be no question of raising wages by more than the increase in profits, because such a policy would at once make production unprofitable for certain undertakings and would cause a fresh decline in business.

But it is also questionable whether a modest rise in wages within the limits of the increase in profits is justified. As we already know, such a rise runs counter to the economic laws of the labour market, and could only be justified as part of a general economic policy in which an increase in the purchasing power of the masses is regarded as desirable. But the argument of mass purchasing power too is not at first sight favourable

[1] It may be objected that in the years immediately preceding 1929 there were increases in wages in spite of the existence of unemployment on a fairly large scale. That is true of certain countries, notably the United States and Germany. The fundamental difference is that unemployment was then in general incomparably lower than the level that must be expected in the future, and also that during previous recovery periods there were times when unemployment disappeared almost entirely both in the United States and in Germany.

to the workers. [1] It is a well-known fact that during every recovery period the ratio of wages to the whole national income falls, and consequently the relative importance of the workers' expenditure declines, though without necessarily checking the process of recovery. It is true that this fact is not without importance for the extent of a subsequent depression, but at present we are still waiting for the upward movement to begin, and it is rather premature to begin worrying about the next depression when we have not yet recovered from its predecessor. For the moment we must pay special attention to the experience of past recovery periods. These indicate that for a limited period a relative decline in the purchasing power of the masses of the population does no great harm. The reason for this is that in periods of recovery there is rapid extension of industrial plant. If wages are comparatively low and profits high, the result is not necessarily a fall in aggregate demand in the national economy ; it only means that a larger proportion of the demand will be for producers' goods instead of for consumers' goods. There would be a possible argument in favour of raising wages only if we could assume that in the immediate future the demand for machines, tools, and buildings due to increased profits could not replace the demand for everyday commodities of the masses of the population to the same extent as in the past.

Let us first consider the beginning of the future recovery period as we have conceived it. There is a gradual increase in the volume of employment, and at the same time industry is becoming more profitable. Is it in the interests of the workers and of the general economy that the whole of the fruits of this improvement should at once be handed over to the workers ? There are two main facts to be borne in mind. If the increase in demand is due to one of the reasons enumerated on page 361 above—because new dwellings are being built, or more and more undertakings have decided to renew their plant, or a wave of optimism has passed over the country and encouraged factories to increase their stocks, or the State has spent large sums on public works—whatever the reason may be, there is an increase of purchasing power in the national economic system. At what

[1] There are of course a number of more or less amateurish economic theories that consider a rise in wages justified in any circumstances. Most of them, unfortunately, cannot survive critical examination.

point it has entered the system is immaterial for our present purpose ; the one important thing is that it should move onwards, representing as it does at every step a new demand for commodities and an increase in the volume of employment. Anything that might interrupt its flow would be detrimental to the national economy ; every measure that hastens its progress would be of advantage. This is the point of view by which wage policy must be guided. If at the beginning of the recovery period a levy is made on the increased profits of industry by an appropriate wage policy, the effect at first will only be that the same aggregate income is redistributed to the greater advantage of the workers. But the probability is that at the same time the general economic situation will also be favourably affected. The period we are here discussing is still suffering from a lack of optimism among industrialists in general. Even if a few firms have decided to increase their expenditure, it is by no means certain that others, which find their sales increasing owing to the greater initiative of the former, will follow the example of these pioneers. Increasing profits are not necessarily translated immediately into an increased demand for commodities. Nor do increased profits always lead directly to an increase in the income of shareholders, for it is well known that dividend policy and actual profits do not always exactly agree. After a severe depression many firms may consider it wiser to increase their liquid reserves of capital ; but if the new profits are used for this purpose, they lie idle, and the flow of new purchasing power is interrupted by so much. If the profits are passed on to the shareholders in the form of dividends, it must again be presumed that the expenditure of the shareholders on consumers' goods will lag behind the increase in their incomes, for the more well-to-do classes of society do not adapt their way of life to every slight fluctuation in their incomes.

The reverse is the case with the poorer classes. No one can doubt that every additional cent earned will lead to a fresh purchase in a few days, for the proportion of savings among the workers is too low to matter in this connection. Wages are not hoarded ; they are the form of income that circulates most rapidly. A rise in wages paid out of the increased profits will —if it has no other harmful effects—speed up the circulation of the additional purchasing power, and may thus accelerate the economic recovery. This was one of the strongest arguments which, more or less clearly expressed, lay behind the policy of higher wages in the United States after the economic revival of 1933.

But there are some conflicting considerations. The argument of more rapid expenditure is concerned with the circulation of the purchasing power set in motion by the first signs of economic expansion. Figuratively speaking, it is not concerned with the breadth of the stream of new demand, but only with its speed: the faster this stream flows the greater will be the increase in sales and in production. But the breadth of the stream is also of importance, and it too depends on the profit-making capacity of industry. So far we have been considering the attitude of industry during this early revival period as purely passive, except in the case of the pioneer firms which, together with the State and other public authorities, increase their expenditure. Industry has been portrayed as meeting the increased demand but doing nothing else itself to increase its own production. But some such further step is necessary if a slow and gentle economic improvement is to gain strength and certainty. If undertakings increase their production by more than is needed to meet the preceding rise in demand, this broadens the stream of supplementary purchasing power. The suggestion that undertakings might increase their production beyond the actual rise in demand may sound somewhat fantastic, and it may be objected that this would lead to renewed over-production and a drop back into the depression. The objection would be valid if the process were too precipitate; otherwise the process is not only possible but is indeed one of the most important characteristics of every upswing, and has probably never been of such importance as in the present case. Increasing production is, in fact, equivalent to additional purchasing power; if output is increased, so also is the expenditure on wages and other costs, and this extra expenditure is transformed into demand for the extra commodities that are being produced. This simultaneity in the rise and fall of the supply of and the demand for commodities is one of the fundamental conditions for the continued existence of the modern economic system based on exchange, and for the success of any new recovery movement. But the thesis of political economy that an increase in production can, in certain circumstances, create the market for the additional goods produced is no guarantee that this theoretical possibility will actually be realised in practice. It is necessary first to remove the psychological obstacles that prevent each individual firm from increasing production until there has first been a rise in demand (although an increase in the production of all firms would lead to an increase in demand). The best means of doing this is by increasing profits. Rising profits are taken by every undertaking as a sign that the market situation has improved, so that if more is produced there is a good chance of finding a market for it. Moreover, an increase in production thereby becomes more profitable, for every additional unit of production sold brings in more than before. And, finally, rising profits are the basis for a change of outlook, stimulating business initiative and a spirit of enterprise and thus inducing firms to make that expenditure on new plant or technical improvements that is so necessary for business recovery.[1] Here we have the argument against the neutralisation of the first improvement in profits.

There is thus a choice between two arguments, the one favouring the speeding up of the circulation of supplementary purchasing power and the other stressing the incentive given by rising profits at the beginning of the recovery period. It is quite obvious that the two opposing views as to the desirability of raising wages are derived from two entirely different series of effects flowing from that one cause. In such a case, the only way to decide is to determine which of the two effects of a rise in wages is the stronger. It must not be forgotten that we are here dealing solely with conditions at the beginning of a revival of production. The progress made is therefore still very moderate, the increase in profits not very great, so that only a very modest rise in wages could be contemplated. This of course reduces the social importance of the measure, but it is also decisive from the economic point of view. Wages could be raised by only a very small percentage, and only an infinitesimal fraction of the national income could be transformed from profits into wages ; the increase in the rate of circulation of aggregate purchasing

[1] The decisive element in this psychological factor is not so much the sum total of the profits as the percentage return on capital. This return may be increased either by earning more profit or by lowering the capital value. One of the most important facts about any depression is that the profitableness of an undertaking can be improved by this latter method—by reorganisation, writing down the capital, etc. This is done only partly at the expense of the nominal value of the plant, and also partly (in the case of fixed-interest-bearing securities) at the expense of the capitalists' income, and not at the expense of the workers. (For this suggestion and for several valuable corrections the author is indebted to Dr. H. Staehle, Geneva, who kindly read and criticised the manuscript.)

power resulting from this insignificant change from income spent slowly to income spent rapidly would be correspondingly slight. But from the point of view of the profitable working of industry and all the consequences that spring from it, this fraction of the national income is of decisive importance, for profits never represent more than a very small part of the cost of production, and an increase in wages of 5 per cent. may in the present situation easily wipe out profits, or at least cut them in half. The negative effect of a rise in wages during the first signs of recovery would therefore seem likely to be much stronger than the favourable influence exerted by it simultaneously. It is probable that to raise wages in these circumstances would hinder rather than help the process of recovery.

So long—but only so long—as the first hesitating steps are being taken out of the morass of a prolonged depression, it would be a rash policy to raise wages. This assertion applies—and the point cannot be too strongly emphasised—only to that state of affairs in which the majority of industrial undertakings have not yet definitely crossed the line below which they are producing at a loss. Once this limit has been passed, the position with regard to wage policy is quite different. If most undertakings are no longer struggling against losses and if the increase in production and sales, however slow it may be, has become a steady and unswerving process—if, in short, the business trend is undoubtedly upwards, then the fact that there are still vast hordes of workers unemployed can no longer be an insuperable obstacle to arise in wages. We have already found it impossible to hold firm to the abstract principles of wage theory, which treats wage movements as if they depended exclusively on whether there is a shortage or a surplus of labour on the market. If wage policy were to follow these principles it would have to refrain from any thought of raising wages even long after the recovery process was securely and steadily advancing. The wage problem cannot however be studied solely in relation to the mechanism of free competition on the labour market, for wage policy is a part of general economic policy. In this it resembles, apart from obvious differences of detail, credit policy. On the money market the play of supply and demand at any given moment may fix the rate of interest at a figure that is perfectly correct and unassailable from the point of view of the abstract theory of markets, which considers *only* the direct relationship between supply and demand. Yet the State often decides to alter the level of interest for other reasons, because it can see not only the direct but also the much more complex indirect effects of this level, which are much more important for the economic life of the country, and therefore also for that section of it consisting of the money market, than strict adherence to the normal rules of the market. But the decision to depart in this fashion from the principles of a free economy should not be taken unless there are strong reasons of economic policy in favour of it. In the writer's opinion strong reasons of this kind do exist in the case of wages at the moment when the economic system passes from the stage of hesitating first attempts at expansion to the stage of a definite upward trend. For in that phase it is no longer a question of whether industrial activity is sufficiently profitable to be once more worth while, but of whether its profitableness is to go on being steadily increased.[1] And it must increase continuously if sales continue to increase while wages remain unchanged. The law of diminishing costs per unit of output will remain operative so long as undertakings are not working to capacity—i.e. are not producing the quantity of goods they were originally built to produce—and full capacity will not be reached for some considerable time when the revival is a slow one. This holds good, of course, if the prices of industrial products remain constant ; in the case of continuous economic recovery there may however be a slight rise in prices.[2] The maintenance of wages at their existing level would then be equivalent to an increase in the proportion represented by profits in the price of manufactured articles and a fall in the share of the national income received by the workers as income.

The next question is whether there is any economic justification for such a course. The usual first argument in favour

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[1] It is naturally difficult to draw the line between a state in which the profitableness of industry cannot stand any further reduction and the state in which profits rise above that level. There is no need to wait until every undertaking shows a profit ; all that matters is that the bulk of industry should be working at a profit. Wage policy should allow for the variety of conditions by differentiating wages much more than has generally been done in the past. Whether the majority of undertakings have or have not reached the stage of showing a reasonable profit will always be a matter for dispute among the groups concerned. No definite criteria can be proposed here ; this is one of those cases that can be correctly decided only by a sound instinctive appreciation of the real economic situation.

[2] No account is here taken of a fall in prices, which the author considers improbable in the present psychological situation. If prices did fall, the argument for raising wages would break down. There would then be a rise in real wages instead of in nominal wages.

of a relative increase in income from investments is that such an increase promotes the formation of capital. But is this a valid economic argument at the present juncture ? This is a point on which general statements are particularly dangerous, for there are in fact a number of countries—Central Europe offers the best example—in which an increase in the liquid capital of the country is an essential preliminary for any real economic recovery. The present line of thought is applicable to them only with reservations ; it applies essentially to the conditions in the great countries of the West, on which general economic revival must primarily depend. But in these countries there is no shortage of capital. Adequate profit for industrial production is as much needed there as elsewhere, but not especially to promote the formation of capital.

But there is another, and perhaps more important, side to the question. The great countries of the West have plenty of floating capital ; they have also sufficient fixed capital in the form of machinery, plant, and means of transport to enable them to carry on production on a much larger scale than at present. This is the point in our argument at which the question of the present surplus-producing capacity of industry with its effects on the economic situation comes into the foreground. It is probable that this excess of potential producing power over the actual level of production was not so great in any depression of recent decades as it now is. There is, it is true, out-of-date plant that should be replaced ; there are also quite recent technical discoveries that are so profitable that they can be put to practical use in spite of the superabundance of productive plant. But against this must be set the fact that the years preceding 1929 were marked by the most intensive capital expenditure of modern times, that much of the machinery of production is new, and that its capacity is still far in excess of market requirements. This fact, as already pointed out, will not only be an obstacle to the beginning of the upswing, but will also militate against its continuance. There are many reasons for believing that in the coming period of increasing prosperity the need for capital investment will be relatively less than in previous similar periods. This is, of course, only a conjecture, as all statements about the economic future must be. If it were not substantiated, and if, for instance, a drastic inflationist policy led to a marked wave of investment, our argument would no longer hold. But our conjecture rests not only on the probability that the process of recovery from the present depression will be slow in every department of economic life. In a period that is still so much oppressed by a feeling of insecurity about the future all forms of economic initiative which require long-term capital investments are likely to suffer with especial severity. Moreover, in previous depressions there was always a factor that helped to overcome the lethargy on the investment market, namely, the appearance of new industries, as, for instance, the electrical industry at the beginning of the present century. To-day there is no sign of any revolutionary technical advance, radically affecting wide domains of industry, such as also dominated the nineteenth century.

One important conclusion concerning wage policy follows from this reasoning. It was pointed out above that during a normal period of rising prosperity there was no objection to an increase in the proportion of profits going to the owners of unearned income, because this was accompanied by a marked increase in the expenditure on means of production. But there is no certainty at present that this increase will occur on the same scale in the future. If, therefore, wages were kept constant during a period of steady economic improvement there would be a continuous rise in profits, with no guarantee that these higher profits would be transformed into expenditure. But the hoarding of profits, the immobilisation of circulating purchasing power, is the worst conceivable menace to economic recovery. *At the present moment there is no longer any reason against an appropriate rise in wages.* The argument that a rise in wages would destroy the initiative of industrialists, which is valid at the very beginning of a revival, no longer holds good, for rising wages cannot now compromise the profitable working of industry; they can only prevent profits from continuing to increase indefinitely. It may be suggested that the activity of industry is proportional to its profits. This is true within certain limits, but these limits are reached as soon as unearned income becomes too great for it to be possible to count with any certainty on its being fully expended.

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No rise in wages until there is a real improvement in the economic situation and the business cycle is definitely on the up-grade—surely, it may be suggested, a sorry conclusion from the social point of view. One would certainly wish that part at least of the losses suffered by the workers in recent years should be more quickly made good. But in the long run it is more disappointing and more dangerous for social policy to follow illusory aims than to face facts soberly, however great the resulting restrictions in regard to immediate demands. And if the considerations set out above have shown how far the possibility of improving the position of the workers depends on the movements of the general economic situation, the view expressed may perhaps diverge in principle from the ideas of the older social policy, but really seems to be self-evident in a period of deep economic depression. The greatest hope at present of securing the economic well-being of the masses of the population lies not in measures to control the level of wages but in active measures of general economic policy to overcome the depression itself.