

Deferred Pay: The Keynes Plan

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Underlying most current controversy as to methods of war finance and the adjustment of wages to rising prices is the vital question who is to pay for the war. In what proportions is the cost of the belligerents' war effort and the neutrals' defence preparations to be shared among the different groups within each community concerned? Of the contributions so far made to the discussion of this question, one of the most illuminating and at the same time one of the most novel is a recent book by Mr. J. M. Keynes. The proposals put forward in this book have aroused widespread interest not only in Mr. Keynes's own country but elsewhere, and the criticism and comment to which they have given rise throw light on some of the central issues of social policy in wartime. The International Labour Office believes, therefore, that the account of Mr. Keynes's proposals and the comment on them which is given in this article will be of interest to readers of the International Labour Review.

THERE can be no economic question of greater importance to working men at the present time than the methods by which war and defence expenditure are financed. This is not because the particular methods chosen can affect to any great extent the basic economic objective of any country which finds itself at war or in danger of attack; for this objective must always be to apply the greatest possible proportion of its productive resources to the prosecution of war or the strengthening of defence, and whatever methods of finance be chosen they must serve this end. The importance of the choice lies in the fact that it will go far to determine who actually bears, both now and in the future, the real burden of the war effort.

It is for this reason that Mr. J. M. Keynes's recent pamphlet *How to Pay for the War*¹ deserves to be studied closely by workers' leaders not only in Great Britain, to the special problems of which the pamphlet is addressed, but in all countries which find their living standards menaced by the demands and threats of war. Mr. Keynes's aim is not merely to provide a solution for a financial problem but "to snatch from the exigency of war positive social improvements". The scheme he proposes includes "universal family allowances in cash, the accumulation of working-class wealth under working-class control, a cheap ration of necessities and a capital levy (or tax) after the war", a combination which he believes "embodies an advance towards economic equality greater than any which we have made in recent times" (pp. iii-iv).

In the pages which follow an outline is given of Mr. Keynes's analysis and proposals; and to this is added a brief discussion of some of the main features of his plan.

THE CHARACTER OF THE PROBLEM

National output, it is assumed, will be raised to the highest figure which resources and organisation permit. In addition there will be a certain quantity of imports. From the total must be taken the goods exported and the requirements of war. What is left is the amount that is available for civilian consumption. Alternatively the requirements of the civilian population may be fixed and only what is left over be devoted to war uses. In practice what actually happens is likely to be compromise between the two methods. In any case there will be a certain definite amount available for civilian consumption. In the interests of the national war effort the size of this amount must be a matter for governmental decision; it cannot be allowed to be influenced to any important extent by what consumers earn and spend.

This, Mr. Keynes points out, is a great change from peacetime experience. Usually production is below capacity; so that if the amount of money people have to spend increases

¹ London, Macmillan & Co. Ltd., 1940, pp. vii + 88, 1s. Except where otherwise indicated the quotations throughout the present article are from this book, and in each case the page reference is indicated in brackets.

more will be produced and there will be more to buy. When men work harder and earn more they can normally increase their consumption in not much less than the same proportion. "In peace time, that is to say, the size of the cake depends on the amount of work done. But in war time the size of the cake is fixed. If we work harder, we can fight better. But we must not consume more" (p. 4).

Since in wartime the size of the cake is fixed, each individual who is able to increase his consumption by spending more does so only at the expense of other people. If all alike spend more no one benefits. For prices will rise just enough for the extra money spent to be used up by the extra cost of what there is to buy.

In actual practice some members of the community must refrain from exercising their power to increase their spending. "Unless the whole cost of the war were to be raised by taxes which is not practically possible, part of it will be met by borrowing, which is another way of saying that a deferment of money expenditure must be made by someone. This will not be avoided by allowing prices to rise, which merely means that consumers' incomes pass into the hands of the capitalist class. A large part of this gain the latter would have to pay over in higher taxes; part they might themselves consume thus raising prices still higher to the disadvantage of other consumers; and the rest would be borrowed from them, so that they alone, instead of all alike, would be the principal owners of the increased National Debt, — of the right, that is to say, to spend money after the war" (p. 6).

"For this reason", Mr. Keynes concludes, "a demand on the part of the Trade Unions for an increase in money rates of wages to compensate for every increase in the cost of living is futile, and greatly to the disadvantage of the working class. Like the dog in the fable, they lose the substance in gaping at the shadow. It is true that the better organised sections might benefit at the expense of other consumers. But except as an effort at group selfishness, as a means of hustling someone else out of the queue, it is a mug's game to play. In their minds and hearts the leaders of the Trade Unions know this as well as anyone else. They do not want what they ask. But they dare not abate their demands until they know what alternative policy is offered.

This is legitimate. No coherent plan has yet been put up to them" (pp. 6-7).

The remainder of Mr. Keynes's essay is devoted to the framing of such a plan.

THE CHARACTER OF THE SOLUTION

In wartime, even if there were no increases in the rates of wages, the total of money earnings would be increased considerably as a result of overtime, the increased number of men engaged (both in the fighting services and in civilian employment), and the movement into paid employment of women, boys, retired persons, and others who were not previously occupied. In a war like the present, however, the amount of goods available for consumption will have to be diminished; at the most it certainly cannot be increased above what it was in peace-time.

"It follows that the increased quantity of money available to be spent in the pockets of consumers will meet a quantity of goods which is not increased. Unless we establish iron regulations limiting what is to be sold and establishing maximum prices for every article of consumption, with the result that there is nothing left to buy and the consumer goes home with the money burning his pocket, there are only two alternatives. Some means must be found for withdrawing purchasing power from the market; or prices must rise until the available goods are selling at figures which absorb the increased quantity of expenditure, — in other words the method of inflation.

"The general character of our solution must be, therefore, that it withdraws from expenditure a proportion of the increased earnings. This is the only way, apart from shortages of goods or higher prices, by which we can secure a balance between money to be spent and goods to be bought.

"Voluntary savings would serve this purpose if they were sufficient. . . . But the analysis of the national potential and of the distribution of the national income" of Great Britain which Mr. Keynes sets out in his essay "shows clearly enough how improbable it is that voluntary savings can be sufficient" (pp. 8-9).

Saving, or deferment of expenditure, must therefore be made compulsory. The first provision in Mr. Keynes's plan

is designed accordingly "to determine a proportion of each man's earnings which must be deferred ; — withdrawn, that is to say, from immediate consumption and only made available as a right to consume after the war is over. If the proportion can be fixed fairly for each income group, this device will have a double advantage. It means that rights to immediate consumption during the war can be allotted with a closer regard to relative sacrifice than under any other plan. It also means that rights to deferred consumption after the war, which is another name for the National Debt, will be widely distributed amongst all those who are forgoing immediate consumption, instead of being mainly concentrated, as they were last time, in the hands of the capitalist class.

"The second provision is to provide for this deferred consumption without increasing the National Debt by a general capital levy after the war.

"The third provision is to protect from any reductions in current consumption those whose standard of life offers no sufficient margin. This is effected by an exempt minimum, a sharply progressive scale and a system of family allowances. The net result of these proposals is, to increase the consumption of young families with less than 75s. a week, to leave the *aggregate* consumption of the lower income group having £5 a week or less nearly as high as before the war (whilst at the same time giving them rights, in return for extra work, to deferred consumption after the war), and to reduce the aggregate consumption of the higher income group with more than £5 a week by about a third on the average.

"The fourth provision, ... rendered possible by the previous provisions but not itself essential to them, is to link further changes in money-rates of wages, pensions and other allowances to changes in the cost of a limited range of rationed articles of consumption, an iron ration as it has been called, which the authorities will endeavour to prevent, one way or another, from rising in price " (pp. 10-11).

OUTPUT CAPACITY AND THE NATIONAL INCOME

Mr. Keynes then goes on to estimate for Great Britain the maximum current output that can be organised from available resources of men, plant, and materials, the rate at which foreign reserves can safely be drawn upon, and how

much of the resulting total will be used up by the war effort. To facilitate the calculation his estimates are made in terms of pre-war prices.¹ By absorbing a considerable proportion of unemployed workers, by bringing boys, women, and retired or unoccupied persons, into employment, and by more intensive work and overtime, the pre-war national output of £4,850 million can, he estimates, be increased (despite withdrawals to the armed forces and other unfavourable factors) by about 17½ per cent., or £825 million. In addition some £450 million of what would normally be spent on new investment and on making good current depreciation could be diverted to Government purposes. Finally a contribution of up to £350 million could be drawn from the sale of gold and foreign investments and from borrowing abroad. Altogether this yields a total of resources for additional Government requirements (above those of peace-time) and current private consumption of £1,625 (£825 + £450 + £350) million a year.

The additional Government expenditure will, however, he estimates, be in the neighbourhood of £1,850 million.² This means that there will have to be a reduction of some £175 million below the pre-war rate of consumption for the community as a whole.³ It is necessary therefore to withdraw from consumption £825 million of increased incomes (earned in producing the output of that amount) plus £175 million of incomes previously spent — that is, £1,000 million in all.

The imminence of this problem has, Mr. Keynes suggests, been obscured by the fact that after six months of war there still persists a substantial volume of statistical unemployment. But "this does not mean we are still in the Age of Plenty. It means that the Age of Scarcity has arrived *before* the whole of the available labour has been absorbed" (p. 18). No doubt output will be increased in the future, but this will take time. So far, moreover, Government

¹ Mr. Keynes points out, however, that by January 1940 wholesale prices had risen by 27 per cent., the cost of living by 10 per cent., and wages by perhaps 5 per cent., so that the figures he gives should be increased by nearly 10 per cent. to conform to the wage and price levels current at that date.

² The period to which the estimate applies appears to be the year ending 31 March 1941.

³ Actually, according to the figures quoted above, the reduction would be £225 million (£1,850 million minus £1,625 million), but as Mr. Keynes uses the figure of £175 million this figure is quoted above. The particular figure taken does not in any case affect the main argument.

demand has increased though private consumption has not sufficiently diminished. The deficiency has been met by drawing on stocks of commodities and on foreign resources and working capital. "The task of adjusting private expenditure to the supply which will be available is, therefore, more urgent than appears on the surface. It is not true that we can postpone action until after full employment has been reached" (p. 19).

CAN THE RICH PAY FOR THE WAR ?

Of the £1,850 million increase in Government expenditure Mr. Keynes estimates that £150 million could be taken out of accruing depreciation not made good at home and £350 million from assets and borrowing abroad. This leaves £1,350 million to be raised from additional taxes and from new savings (including normal savings), voluntary or involuntary. At least £400 million can be expected from voluntary savings, leaving some £950 million still to be found.

Could the rich provide this sum ? To answer this question Mr. Keynes estimates the probable total incomes and voluntary savings in each of three income groups : below £250 a year, £250-£500, and above £500. The net totals after deducting voluntary savings and pre-war taxes are £2,895, £615 and £1,045 million respectively. The conclusion reached is that "if everyone with more than £500 a year had the whole of his income in excess of that sum taken from him in taxes, the yield would not be nearly enough, being £620 million or only two-thirds of the Government's requirements" (p. 24).

"Yet this suggestion", Mr. Keynes considers, "is a wild exaggeration beyond what could be expected from our fiscal system. Indeed taxation on this scale would involve such wide-spread breaches of existing contracts and commitments that the taxable incomes themselves would be largely reduced. An important part of these incomes is spent on rates and other purposes which do not increase personal consumption, on current resources, the alternative uses of which are much less valuable, and on payments to dependants. It follows that an important contribution must be obtained one way or another from the income group below £500 a year.

"Nor is it practicable to put the exemption limit at £250 a year. There are about 2,430,000 persons with incomes above this level. If the whole of the excess of their remaining incomes above £250 was taken from them, namely £1,010 million and if this caused no reduction in the incomes by repercussion (which is far from the truth), it would only just exceed the Government's requirements. If the cost of the war is to be met by the income group above £250 a year, it would mean taking from them in savings and taxation (new and old) about three-quarters of their total war-time incomes, leaving them with less than a quarter of their incomes for their own consumption.

"In the light of these figures it is not sane to suppose that the war can be financed without putting some burden on the increased war incomes of the class with £5 a week or less. For this income group accounts for about 88 per cent. of the population, for more than 60 per cent. of the total personal incomes of the country after allowing for war increases (due to greater output but allowing nothing for higher wage-rates) and deducting pre-war rates and taxes, and for about two-thirds of current consumption. Moreover the incomes of this group will have been increased on the average by some 15 per cent. as a result of the war. Is it seriously expected that those with less than £5 a week will be allowed to increase their average consumption by 15 per cent., while all those with more than £5 a week will be left on the average with only a quarter of their incomes to consume? The only question is, therefore, how large the contribution of this class must be, and how it can be obtained with least sacrifice and most justice.

"If we have a deliberate plan, considerations of social justice can be weighed and considered. Without such a plan (as at present) they go by default" (pp. 25-26).

MR. KEYNES'S PLAN

Of the £950 million of incomes in private hands which must not be spent but must be diverted to the finance of the war some £500 million might be taken by taxation. The idea that the remaining £450 million could be raised by voluntary savings without any aid from inflation Mr. Keynes dismisses as chimerical. "The additional savings would

have to come largely from the income group with £5 a week or less and would require a change in their habits of expenditure for which there is no evidence" (p. 29).

Whatever method is adopted the amount by which the potential expenditure of the lower income groups has to be curtailed will be more or less the same. "Inflation", Mr. Keynes considers, "will be the most burdensome alternative, since this will inevitably bring some advantage to the entrepreneur class, and might cost the worker 20 per cent. in terms of the real value of his earnings. Inflation will also be the most burdensome on the smallest incomes, — a defect it shares with a general sales-tax. New taxes, such as a sales-tax or a wages-tax, or old taxes aided by inflation are alike in that they finally deprive the workers of the benefit of their earnings from their heavier burden of labour. They will work harder, but, as a group, they will *never* derive any personal benefit from it" (p. 29). This, however, is what will inevitably happen if the usual methods are followed.

In the alternative policy which Mr. Keynes proposes the main element is a system of deferred pay. The community as a whole cannot consume *now* the equivalent of their increased war effort, for the results of that effort are used for war purposes and cannot supply increased consumption. Those who make the effort, therefore, must either forego the equivalent consumption altogether, or — and it is this that Mr. Keynes proposes — they must *postpone* it.

The remainder of Mr. Keynes's proposals are designed to ensure that most of the burden of paying for the war falls on the richer classes and that special reliefs are allowed to the poorer. Of the £500 million which is to be raised by additional taxation the bulk should come from those with incomes over £250 ; and the main part of the contribution of the lower income groups should take the form, not of foregoing income outright, but of merely deferring it. To ensure that adequate minimum standards are maintained a family allowance of 5s. a week should be paid in cash for each child up to the age of 15.¹ In addition a minimum ration of consumption goods should be made available at a low fixed price. This minimum ration Mr. Keynes suggests "should not comprise all the articles covered by the cost of living Index, but should be restricted to a limited list of necessities available in time

¹ There is at present no national system of family allowances in Great Britain.

of war. Nor should any absolute undertaking be given as to future prices. It should be agreed, however, that in the event of any rise in the cost of the minimum ration, the Trade Unions would be free to press for a corresponding increase in wages.

"But it should be an absolute condition of such an arrangement that a scheme for deferred pay should be accepted at the same time, and that the Trade Unions should agree, subject to the above safeguard, not to press for any further increases in money wages on the ground of the cost of living"¹ (p. 33).

So much for the general principles. The details, which Mr. Keynes regards as a question of degree and opinion, can be summarised only very briefly in this article. In general they are designed to ensure that:

"(1) The aggregate real consumption of the group with £5 a week or less should be maintained for as long as possible at or near the pre-war level.

"(2) Those who remain in the lower half of this group are likely to have benefited least, or not at all, from the aggregate increase in war incomes, and cannot afford, therefore, to have any important part of their current earnings deferred if they are to maintain their standard of life.

"(3) Since some rise in the cost of living relatively to wages (though not to total earnings) is inevitable, and since it is impossible under any scheme to avoid individual inequalities of treatment, we should make sure by means of family allowances that the inequality will work out in favour of households with families, so that these will be for certain better off.

"(4) Since the increased war incomes of the lower income groups probably represent increased work to a greater extent than in the case of the higher income groups, the contribution of the former should be mainly in the form of deferment of earnings and the contribution of the latter mainly in the shape of increased taxation" (pp. 35-36).

The general result aimed at in Mr. Keynes's calculations is that the aggregate consumption of the higher income group

¹ "Without these conditions", Mr. Keynes explains, "the weight of purchasing power available in the hands of consumers would render any attempt at price fixation excessively dangerous. The low prices for the minimum ration would merely release more purchasing power for use in other directions, which would drive up other prices to an excessive disparity with that of the fixed ration. To attempt to fix consumption prices whilst allowing an indefinite increase of purchasing power in the hands of consumers would be an obvious error" (pp. 33-34.)

(that is, those with incomes above £250 a year) should be reduced by fully a third and the aggregate consumption of the lower income group not at all.¹ The scheme would thus "effect a considerable redistribution of incomes in the direction of greater equality" (p. 38).

To achieve this result Mr. Keynes proposes: that the system of children's allowances under the existing income tax should be abandoned and replaced by a flat payment of 5s. per week per child, both for income tax payers and for the insured population; that a basic minimum income of 35s. a week in the case of unmarried men and 45s. in the case of married men be free of deferment; that a percentage of all incomes in excess of this basic minimum be paid over to the Government partly as direct taxes and partly as deferred pay, the combined percentage taken rising steeply as the level of income increases; that the appropriate part of a man's withheld income be used to discharge his income tax if any and the balance be credited to him as a blocked deposit carrying interest at $2\frac{1}{2}$ per cent. compound; that each individual be allowed considerable choice as to the institution—such as a friendly society, a trade union, or the Post Office Savings Bank—in which his deferred pay should be deposited; and that deferred pay be released when necessary to meet certain pre-war commitments (such as life insurance premiums and hire purchase instalments), death duties, new life insurance or endowment policy premiums, and certain family and personal emergencies such as illness. Finally, "men on active service might have their economic position made a little more equal to the position of those remaining in civilian employment by being credited with an appropriate blocked deposit proportional to their length of service. A 'veteran's bonus' is a peculiarly fit obligation for discharge by a capital levy on wealth" (p. 50); and excess company profits, after payment of taxes, might also be placed in blocked deposit.

The percentage of income to be withheld in the standard case of a married man with no young children would range from nil at an income of 45s. a week to 6 per cent. at 55s., $19\frac{1}{4}$ per cent. at 100s., 21 per cent. at £300 a year, 27 per cent. at £500, 35 per cent. at £1,000, $53\frac{1}{2}$ per cent. at £5,000, and

¹ It should however be noted, though Mr. Keynes does not draw attention to the point, that this does not mean that the average consumption of individuals in this group would be maintained; for the total members in the group will presumably increase.

85 per cent. at over £50,000. The amounts of deferred pay would range from nil at 45s. a week to 3s. 6d. at 55s., 15s. 10½d. at 100s., £49 a year at £300 a year, £135 at £1,000, £630 at £5,000, and £4,133 at £100,000. The amounts of income remaining after taxation and deferment would be unchanged at an income of 45s. a week, 51s. 6d. from an income of 55s., 80s. 9d. from 100s., £236 a year from an income of £300, £647 from £1,000, £2,315 from £5,000, and £15,099 from £100,000. Altogether a married man with two young children would actually have more left in cash for immediate consumption for all rates of earnings up to 75s. a week and a married man with three young children would have more left for all rates up to nearly 95s. In addition family men would have substantial amounts to their credit in deferred pay.

Save for the exceptions noted, the blocked deposits would not be available for use "until after the war when they would be released by a series of instalments at dates, not unduly delayed, to be fixed by the Government. Meanwhile they should not reckon in calculations arising out of the Means Test or eligibility for old-age pensions or the Capital Levy to be proposed below or the like.

"The appropriate time for the ultimate release of the deposits will have arrived at the onset of the first post-war slump. For then the present position will be exactly reversed. Instead of demand being in excess of supply, we shall have a capacity to produce in excess of the current demand. Thus the system of deferment will be twice blessed; and will do almost as much good hereafter in preventing deflation and unemployment as it does now in preventing inflation and the exhaustion of scarce resources. For it is exceedingly likely that a time will come after the war when we shall be as anxious to increase consumers' demand as we are now to decrease it. It is only sensible to put off private expenditure from the date when it cannot be used to increase consumption to the date when it will bring into employment resources which otherwise would run to waste.

"If the deposits are released in these circumstances, the system will be self-liquidating both in terms of real resources and of finance. In terms of real resources it will be self-liquidating because the consumption will be met out of labour and productive capacity which would otherwise run to waste. In terms of finance it will be self-liquidating because it will

avoid the necessity of raising other loans to pay for unemployment or for public works and the like as a means of preventing unemployment." (pp. 45-46).¹

If, however, the war continues for two years or longer, the National Debt will reach an unmanageable figure. In such circumstances a capital levy (or tax) would be advisable. For this reason, and to overcome any doubts as to the possibility of repaying the blocked deposits, Mr. Keynes suggests that an undertaking be given that a capital levy will be enforced after the war to bring in an amount sufficient to discharge the liability in respect of deferred pay. The two should not be synchronised ; for it would be best to withhold the deferred pay until the onset of serious unemployment, while this would be the worst possible time for the capital levy. " If the levy is to be paid in a lump sum, it should be discharged at the earliest possible date after the close of the war, especially if temporary boom conditions seem imminent. But it might be preferable, as facilitating collection and greatly lessening the disturbance, to collect it in a series of instalments over a period. This procedure would have the special merit that it might pave the way administratively for a permanent capital tax which would be a valuable addition to our fiscal machinery and has certain important advantages over income tax." (p. 48).

For the scheme as a whole, Mr. Keynes claims that it offers to the trade unions "great and evident advantages compared with progressive inflation or with a wages tax. In spite of the demands of war, the workers would have

¹ Mr. Keynes has since suggested that the system of deferred pay, to be released later as a means of combating unemployment, would be equally desirable in peacetime. " I think of it ", he writes, " as a first instalment of a comprehensive social policy to regulate the general rate of spending so as to avoid the disastrous alternations of boom and slump which will otherwise continue to undermine the foundations of society. " Such a policy " may come to be thought of as marking the line of division between the totalitarian and the free economy. For if the community's aggregate rate of spending can be regulated, the way in which personal incomes are spent and the means by which demand is satisfied can be safely left free and individual. " (Letter to *The Times*, 10 April 1940). This proposal raises issues too broad and complex to be dealt with here, but three brief comments may be offered. First, it would obviously be incomparably more difficult to secure public acceptance of the principle of deferred pay in peacetime than in time of war. Second, the effectiveness of any particular scale of deferment would depend largely on the extent to which economic fluctuations originate within the country concerned ; a scale appropriate to Great Britain might have little effect in such countries as Argentina, Australia, or New Zealand, and the scale required to have any marked influence in these countries might be so high as to be quite impracticable. Third, there may be other ways of regulating " the community's aggregate rate of spending " which would be at once more effective and more acceptable.

secured the enjoyment, sooner or later, of a consumption fully commensurate with their increased effort ; whilst family allowances and the cheap ration would actually improve, even during the war, the economic position of the poorer families. We should have succeeded in making the war an opportunity for a positive social improvement. How great a benefit in comparison with a futile attempt to evade a reasonable share of the burden of a just war, ending in a progressive inflation ! ” (p. 34).

COMMENT ON THE PLAN

Though Mr. Keynes's proposals have aroused keen interest in Great Britain — and indeed elsewhere — they have not as yet gained the full support even of those groups of the community whose interests they are designed to serve. It was not to be expected that they would receive either speedy or unqualified acceptance, and the fact that opinion is still divided — and indeed not clearly crystallised — does not mean that some modification of the Keynes plan may not eventually receive more general support. Apart from such points as are discussed below there is, it may be suggested, one general question the answer to which will have an important bearing on the prospects of the plan. This is the extent to which opportunities can be afforded for the effective participation of the workers' organisations both in the elaboration of any final scheme and in its actual administration both during and after the war. In any case, the fate of the plan must depend largely on the extent to which it can win the approval of the trade unions ; for so revolutionary a principle as that of deferred pay could not be applied without their concurrence, and the plan as a whole seems unlikely to be adopted, either as it stands or in any form which retains its essential features, without their strong and active support.

For the present, indeed, the principle of deferred pay has been rejected by the British Government. The Chancellor of the Exchequer, in presenting his proposals for the 1940-41 Budget, expressed fears that compulsion would “ kill the voluntary spirit ” and endanger the success of the national savings campaign, that if the Keynes scheme were adopted wages might rise and thus nullify its effects, and that its application would involve serious administrative difficulties.

He therefore preferred to rely on increased taxation and on borrowing from voluntary savings.¹

Though Mr. Keynes's proposals have not yet been adopted, they and the criticism and comment to which they have given rise have thrown light on many of the central issues of social policy in wartime. Certain of the points discussed which are of general interest will be surveyed briefly in the following pages.²

Voluntary Savings versus Compulsory Deferment

One of the main subjects of controversy is the relative merits of compulsory and voluntary savings. Compulsory methods, it has been suggested, accord ill with traditions of democracy and freedom. To impose a system of deferment or "forced loans" would be to discourage voluntary saving, the possibilities of which have not yet been fully explored. The result might be to reduce rather than to increase the total volume of saving. Wage earners in particular, it is argued, might save less under "a compulsory system hedged in by safeguards against inequities and injustices as between one household and another" than under the voluntary system, since the psychological reaction to compulsory levies would be adverse to additional voluntary saving, and consequently "the saving capacity of the household enjoying a temporary and fluctuating accession of income through extra employment and overtime would not be tapped, and it is in these cases, perhaps rare numerically but whose resources are heavy in the aggregate, that the capacity of saving is greatest".³

¹ *The Times*, 24 April 1940, p. 3. The Chancellor announced at the same time that a Bill would be introduced to limit company dividends for the duration of the war. As a result, a substantial volume of company profits will remain undistributed until after the war and will in practice have to be invested in Government securities (no other suitable avenue of investment being open in wartime). The effect will thus be similar to that of Mr. Keynes's proposal, noted above, that the balance of excess company profits after deduction of taxes be held in a blocked deposit.

² The reader who desires to pursue further the subject of war economics and war finance may be referred to the following works on war economics and war finance: A. C. PIGOU: *The Political Economy of War* (London, Macmillan, Revised edition 1940); R. W. B. CLARKE: *The Economic Effort of War* (London, Allen & Unwin, 1940); Geoffrey CROWTHER: *The Sinews of War and Paying for the War* (Oxford Pamphlets on World Affairs, Oxford, Clarendon Press, 1940); André PIATIER: *L'Economie de Guerre* (Paris, Librairie Générale de Droit et de Jurisprudence, 1939); E. M. F. DURBIN: *How to Pay for the War* (London, Routledge, 1939); and E. Ronald WALKER: *War-time Economics, with special reference to Australia* (Melbourne University Press, 1939). There is also an extensive literature in German.

³ Letter from Sir Theodore CHAMBERS in *The Times*, 21 March 1940, p. 9.

To these criticisms Mr. Keynes replies in effect that, while voluntary saving is entirely desirable and is beneficial so far as it goes, it is only by the method of inflation, with all the hardship and inequity inevitably involved, that such saving can be brought about on a sufficient scale.¹ That some rise in prices is to be expected is indeed common ground, for those who advocate reliance on voluntary saving do not claim that it can arrest inflation altogether. The difference in the dimensions of the inflation expected is a difference of degree, but it is one which may be of vital importance to those sections of the community which bear the brunt of rising prices. A special interest attaches, therefore, to Mr. Keynes's analysis on this point. For reasons of space this analysis, which is illustrated by 1914-1918 figures and by estimates for the present time, cannot be given in full here but its general nature can be indicated. "There is", says Mr. Keynes, "no difficulty whatever in paying for the cost of the war out of voluntary savings;—provided we put up with the consequences A Government, which has control of the banking and currency system, can always find the cash to pay for its purchases of home-produced goods. After allowing for the yield of taxation and for the use of foreign reserves to pay for the excess of imports over exports, the balance of the Government's expenditure necessarily remains in the hands of the public in the shape of voluntary savings. That is an arithmetical certainty; for the Government having taken the goods, out of which a proportion of the income of the public has been earned, there is nothing on which this proportion of income can be spent. If prices go up, the extra receipts swell someone's income, so that there is just as much left over as before" (p. 61). The "someone" whose income is increased by rising prices is in general the owner of goods. A large part of his profits will be taken in taxes but "it is likely that a considerable proportion of the balance will be voluntarily saved; not so much because the recipients, being relatively rich, will save more readily, but because the profits will largely belong to companies which will be

¹ Mr. Keynes does refer to another possible method—namely, control of the production or consumption of consumers' goods so comprehensive and so strict as to leave consumers with a significant fraction of their incomes which they would be unable to spend and so would have to save—but dismisses it as an "elaborate, roundabout and wasteful method" of arriving "at the same result as if that fraction of their incomes had been deferred from the outset" (pp.52-53).

disinclined, for various reasons, to distribute the bulk of them in higher dividends but will prefer in the circumstances to save them on behalf of their shareholders" (p. 65). Money wages also will rise after a time lag. Wages and other costs will in fact chase prices upwards but prices will always be a jump ahead. "However much wages are increased, the act of spending these wages will always push prices this much in advance" (p. 66). Moreover, pensioners and *rentiers* with fixed money incomes cannot escape a sacrifice. "It is these time-lags and other impediments which come to the rescue" (p. 66). "Thus, after all, the system of voluntary savings will have worked successfully. That is to say, the money will have been raised 'voluntarily' without an unlimited increase of prices. The only condition for its success is that prices should rise relatively to wages to the extent necessary to divert the right amount of working class and other incomes into the hands of the profiteers and thence into the hands of the Treasury, largely in the form of taxes and partly in the form of extra voluntary savings by the profiteers" (p. 67).

Whether the term "voluntary" is appropriate is, says Mr. Keynes, a matter of taste. "It is a method of *compulsorily* converting the appropriate part of the earnings of the worker which *he* does not save voluntarily into the voluntary savings (and taxation) of the entrepreneur" (p. 69).

If this method is followed, the claims on future consumption and the advantages of security which saved resources afford will be concentrated after this war, as they were after 1918, in the hands of a small class of persons. Under Mr. Keynes' plan they would be distributed widely throughout the community.

Administrative Difficulties

Closely connected with the objection to compulsion as being likely to deter voluntary saving is the criticism that it would involve serious difficulties in administration. It would require, for example, the exact ascertainment of large classes of incomes about which little or no information is at present available. To avoid anomalies and injustice, household as well as individual incomes would have to be taken into account, for "the household and not the individual is the fundamental unit of earning and spending

There is not only an infinite variety of circumstances connected with commitments and dependants as between one household and another, but the needs of the household in monetary terms vary from week to week and are rarely static. One week the aggregate earnings of the household may rise and the next week fall. The commitments towards dependants vary with the coming and going of dependants. There is nothing static about the relationship between needs and resources in the wage earner's household. Mr. Keynes' proposal is to assess deferred pay on the basis of the wages of the individual. This will not fit in with the facts of life. Were such a proposal to be put into force there would be a demand for an adequate 'means test' and indubitably the minds of the people would be turned in the direction of avoidance of the levy."¹ There would consequently be serious difficulties of administration and enforcement, and the system as a whole, like the "means test" under the Unemployment Insurance Acts, might be exceedingly unpopular.

These are undoubtedly serious difficulties. Were the general principle of the plan accepted, some of them, such as the lack of adequate information about individual and household incomes, could no doubt be overcome, and the information collected would be valuable for the planning of social and economic policy not merely during the war but afterwards. Others, however, are of such a character as to suggest that if the Keynes plan or anything closely resembling it is to be applied successfully, it must first be understood and accepted by public opinion, and particularly by organised labour.

The Distribution of the Burden

More fundamental and more difficult to reconcile are the differences of opinion as to how the burden of the war should be distributed among the different income groups. The central question is not so much how to pay for the war as who is to pay for it. Mr. Keynes has been careful here to emphasise that the details of his plan are open to discussion and amendment; almost the only point on which he has insisted is the fact that, although the rich can and should bear by far the greater part of the burden, their total income is not sufficient to cover the whole cost; part of the burden must therefore

¹ Letter from Sir Theodore CHAMBERS in *The Times*, 21 March 1940, p. 9.

fall on those members of the lower income [groups whose income exceeds a necessary minimum. This contention has not seriously been challenged. Criticism has concentrated rather on such points as the particular scale of levies suggested by Mr. Keynes and the proportions in which these levies should be allocated to deferred pay or taxation.

A married man with £4 a week, it is pointed out, would have only £3 7s. 9d. left after deduction of the levy, while a married man with £19 a week would have £12 10s. Why so great a difference, if the aim is to reduce spending power? Again, if the war lasts three years, the group with incomes over £250 a year would get back deferred pay to the amount of £1,050 million, or 55 per cent. of their total income for one year, while the group with incomes of less than £250 would get back only £750 million, or 25 per cent. of one year's income. How can this be reconciled with the aim of reducing inequality? Those with incomes below £250 would have an average of $8\frac{1}{2}$ per cent. of their total income retained in deferred pay; those above £250 an average of 18 per cent. The latter would postpone a larger part of their spending power because they can afford to do so. But does not this mean that they could bear heavier taxation?

Such criticisms as these raise the whole question of the distribution of wealth and income. It is Mr. Keynes's aim to modify this distribution in the direction of greater equality. What his critics contend is that he does not go far enough: the change, they say, should be both greater and faster. On such issues as these no easy agreement is to be expected. On the one hand, the radical changes which war brings in the economic and institutional framework underlying the existing distribution strengthen the case which can be made at any time for modifying that distribution in the direction of reducing inequality; while on the other a balance must be struck, in framing any practical policy, between the disorganisation and social costs involved in any sudden departure from customary conditions and the benefits to be expected from the achievement of greater equality. On all these matters there is clearly room both for difference of opinion and for prolonged negotiation.

The problems involved, it may be noted, are not merely political and ethical but economic as well; for any change in the distribution of income involves transfers of workers

and of other productive resources from one type of production to another. If the incomes of the poor are increased at the expense of the rich, the commodities they will buy will not be the same as those formerly purchased by the rich. How serious the problems of transfer will be will depend both on the magnitude and on the rapidity of the change effected. In wartime, moreover, what matters most for the purpose of maximising war effort is not whose spending is restricted but whether the productive resources set free by the reduction in spending can be adapted quickly to war uses. Redistribution will not serve immediate war needs (save in so far as it improves general morale) unless the resources formerly used to supply the demands of the rich can be used either directly to produce war supplies or indirectly to increase the efficiency (by improving the living standards) of workers engaged in producing such supplies. To stress such points as this is not, of course, to imply that measures of redistribution are either impracticable or undesirable. Such considerations must, however, be taken into account — in addition to the general social consequences involved — in any estimate of the rate at which redistribution may advantageously proceed.

Complementary to the criticism that under the Keynes plan the proportion of the levies on incomes to be taken by taxation is not sufficiently steeply graded is the suggestion that other types of taxation might also be used to a greater extent. One of the proposals most frequently made is that for the duration of the war all profits above a certain level or all excess profits traceable to the war should be taken for the State. This Mr. Keynes describes as a “counsel of perfection” but inadvisable in practice “because it would deprive those who would nevertheless remain in control of their businesses of any incentive towards economy; and the experience of the last war showed that this is liable to lead to great extravagance and waste” (p. 50). A further objection, it might be added, is the possibility that taxation on such a scale as to leave the entrepreneur no opportunity for gain might weaken the incentive to maximum effort. It is, however, a matter of opinion — and perhaps also a matter for investigation — at what point the check on incentives to economy and efficiency becomes serious. To suggest, as is sometimes done, that wage earners should put forth their maximum effort for motives of patriotism and without

asking for wage increases, and to argue at the same time that profit incentives must be maintained for the entrepreneur, is, to say the least, illogical. But whatever be the level at which rewards must be maintained to provide the necessary incentive the case for financing the cost of the war to the greatest possible extent from taxation is so strong that advantage should certainly be taken of every possibility of increasing the revenue from this source. Too much should not, however, be expected from taxes on increased profits, for unless inflation is allowed to develop on a considerable scale — and this, it is urged, should at all costs be avoided — the rise in profits will not be very great.

In addition to more steeply graded income taxes and other taxes designed to diminish unessential consumption, there should, it is suggested by some critics, be an annual tax on capital not merely after but during the war. To those who urge a capital tax as a method of war finance, Mr. Keynes replies that it "would do little or nothing to solve the immediate problem. A Capital Levy on a scale worth having could not be met out of the current consumption of the wealthy. They could only pay it by handing over assets to the Government, the capital value of which would be of no assistance whatever to the immediate financial task. Nothing is of the least use now which does not diminish consumption out of current income; and . . . no expedient can be adequate which allows the increased purchasing power of the lower income groups to materialise in a corresponding increase in their consumption. There is no avoiding a postponement of expenditure on the part of this group, except by inflation which allows them to spend and deprives them of the fruit of spending" (p. 49). The fact, however, that a capital tax would not solve the immediate problem — which is to divert income from current consumption — does not rule out the case for it as a means of diminishing social inequality. To quote one advocate: "A capital levy will not pay for the war; but it could be so used as to limit greatly the opportunities for war profiteering, and it would be an earnest of real preparedness to accept a large measure of redistribution of wealth at the expense of the capitalist class."¹ It might at the same time go far to reassure those

¹ G. D. H. COLE: "Economic Consequences of Mr. Keynes", in *The Tribune*, 29 March 1940, p. 7.

critics who fear that an undertaking to impose a capital levy after the war might not in fact be carried out. As against such possible advantages, however, due weight must be given to the possible repercussions of any substantial capital tax on property markets disorganised by war, the difficulty at such a time of ensuring equitable treatment as between holders of different types of property, and the numerous other administrative difficulties involved. Such difficulties, Mr. Keynes believes, might prove insuperable. Undoubtedly they would call for special measures of a kind which a levy imposed immediately after the end of a war might not necessitate.

Some Implications for Wage Policy

Mr. Keynes's plan is not concerned primarily with the problem of wages. "It is wiser", he thinks, "to deal with it indirectly" (p. 55). If some such scheme as he has proposed is not adopted a significant rise in prices cannot be avoided and real wages will inevitably be seriously reduced. If, however, by the adoption of his proposal for deferment of income, purchasing power is withdrawn from circulation there will be no reason why the vicious cycle of prices and wages should be started by the forcing up of prices at the demand end. "There might", he suggests, in elaboration of a proposal outlined above, "be certain subsidies in part compensation for price increases due to the higher cost of imports and some rise of wages for grades of labour which already had a special claim for an improvement. But the main reason for the development of an acute wages problem would have been removed, and we could safely leave the sequel to the common-sense and public spirit of trade unionists as to what is or is not reasonable in time of war.

"Nevertheless, if a scheme for deferment of pay is adopted, this would make practicable a further measure which might considerably ease the wages problem. For with an adequate proportion of consumers' purchasing power withdrawn, the risk and expense of a deliberate policy to keep down the prices of a limited range of necessities might be no longer prohibitive. I suggest, therefore (contingently on the adoption of a scheme for deferment of pay), that a limited range of essentials, considerably narrower than the list covered by the Ministry of Labour Index Number for the cost of living,

should be drawn up and that the Government (without giving any specific pledge) should do their best to prevent any rise in an index number based on the cost of these articles ; and that on their side the Trade Unions (also without giving any specific pledge) should agree that they will not press for any wage increases *on the grounds of the cost of living*, except in so far as the Government may be unsuccessful in keeping the above index number from rising. This suggestion is in no way essential to our main proposals, but is a further development which these proposals would facilitate " (pp. 56-57). The final sentence of this extract is worth underlining : the proposal to link wages to the prices of necessities is, Mr. Keynes considers, rendered possible by his plan ; but it is not essential.

Elsewhere in his book, Mr. Keynes describes the limited range of necessities to the prices of which wages would be linked as an " iron ration " — a term which has suggested to some critics a type of minimum subsistence that would be incompatible with either the self-respect or the health and efficiency of the wage-earner. Such an interpretation probably does less than justice to Mr. Keynes' intention, but until his proposal is made more specific the suspicions of the critics are likely to persist. It is clear in any case that if the plan as a whole should become at a later stage a subject of actual negotiation a good deal would turn on the interpretation given to details of this kind.

Apart from such comments on particular aspects of the plan, most of the discussion of its implications for wage policy has been concerned with the general question of the proportions in which the cost of the war is to be shared as between wage earners and other groups in the community. As such it has been noted briefly above in the section on the distribution of the burden.

The writer has not as yet seen any discussion of the difficulties which might be involved in the actual application of an undertaking that (with the exceptions noted) wage increases would not be sought on the ground of rising costs of living, or in any attempt to limit wage increases to those " grades of labour which already had a special claim for an improvement ". Yet in practice, it may be suggested, either of these policies would be likely to raise problems of considerable difficulty. It may be, as Mr. Keynes assumes, that

stabilisation of the cost of necessities would remove the main reason for the development of an acute wages problem ; but it is easy to overestimate the influence of the cost-of-living factor in wage negotiations, and an agreement to eliminate all reference to this factor might in practice have little effect at a time when many types of labour are in short supply and the demand for them is keen. For much the same reason an attempt to limit wage increases to workers with special claims for improvement might stand little chance of success unless it formed part of a comprehensive system of regulation covering both wage rates and the movement or engagement of workers.¹ There is not space here to examine the problems involved in the operation of such a system, but it need scarcely be emphasised that they would be both complex and persistent. For their successful solution the full collaboration at all stages of trade union and employer representatives would be essential.

Finally, it may be suggested, there will be other problems of wages besides those referred to which will need attention. In time of war some industries must languish and decline and the wages of their workers may remain or fall unduly low. Two of Mr. Keynes's proposals — family allowances and low prices for necessities — would, it is true, do much to safeguard the position of such workers, and his plan as a whole, by restricting the tendency to inflation, would remove one of the main causes of their distress. It is, however, by no means certain that these measures would be sufficient. Where trade union organisation is weak an extension of existing minimum wage fixing machinery or some new arrangement for this purpose may prove desirable.

CONCLUSION

It will be clear from even so cursory a survey that Mr. Keynes has succeeded in stimulating keen thought on some of the most important issues of the present time. Though opinions are bound to differ as to the merits of parti-

¹ Cf. in this connection the accounts of experience during 1914-1918 given in Humbert WOLFE : *Labour Supply and Regulation*, (Oxford, Clarendon Press, 1923) ; Henry CLAY : "Government Control of Wages in Wartime", in *The Problem of Industrial Relations and other Lectures* (London, Macmillan & Co., 1929) ; and William OUALID and Charles PICQUENARD : *Salaires et Tarifs. Conventions collectives et Grèves. La Politique du Ministère de l'Armement et du Ministère du Travail* (Paris, Les Presses Universitaires de France, 1928).

cular features of his plan and as to the ways in which it might be improved, the concern which it reveals for social justice and the prospects it offers of an approach to greater equality and security and of some reduction of economic instability are such as to command the respect even of its critics.

As its author insists, the plan as a whole must be judged against the possible alternatives. In the list of these, taxation as a source for the whole of war expenditure is scarcely to be included ; for however desirable it may be to rely on this source to the greatest possible extent it would be unrealistic to expect it to cover anything like the whole cost. In a prolonged war the real alternatives to some such scheme as that of Mr. Keynes must be either the regimentation involved in wholesale rationing, price fixing, and wage control, or such a degree of inflation as would bring intolerable hardship to all sections of the workers save the fortunate few whose strategical position might enable them to secure corresponding wage advances. Against such alternatives the advantages of Mr. Keynes's main proposals seem likely, as time goes on, to stand out in increasingly sharp contrast.